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FOREIGN CORRUPT PRACTICES ACT—

OVERSIGHT ORIGINAL

COMPLETED

HEARINGS

BEFORE THE

SUBCOMMITTEE ON TELECOMMUNICATIONS,
CONSUMER PROTECTION, AND FINANCE

OF THE

COMMITTEE ON ENERGY AND COMMERCE
HOUSE OF REPRESENTATIVES

NINETY-SEVENTH CONGRESS

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FOREIGN CORRUPT PRACTICES ACT— OVERSIGHT

WEDNESDAY, SEPTEMBER 16, 1981

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON TELECOMMUNICATIONS,
CONSUMER PROTECTION, AND FINANCE,
COMMITTEE ON ENERGY AND COMMERCE,
Washington, D.C.

The subcommittee met, pursuant to notice, at 9:40 a.m., in room 2123, Rayburn House Office Building, Hon. Timothy E. Wirth (chairman) presiding.

Mr. WIRTH. The subcommittee will come to order.

Thank you all very much for your patience. There is a Democratic Caucus going on now. I had to put in an appearance there.

Today marks the first of a set of hearings on the Foreign Corrupt Practices Act. Most of us remember the mid-1970's in which the country learned that hundreds of major American corporations had paid millions of dollars in bribes and other payments to foreign government officials.

We discovered this after the Watergate Special Prosecutor found millions of dollars in illegal laundered corporate contributions made to the Presidential—Nixon Presidential and other—campaigns.

One commentator called the discovery of foreign payments the second half of Watergate. The effects of these disclosures may have been as far reaching and long lasting as the first half. When the dust settled, more than 450 corporations reported payments of hundreds of millions of dollars to foreign nationals and governments.

At the time many of those involved said the payments made by multinational corporations in foreign countries were merely the local way of doing business and the accepted way of competing with other American and foreign firms. But for most people, there was public outrage and a call for immediate and firm action to end what was commonly perceived as simple bribery.

Although the SEC was able at the time to bring about disclosures of the payments by public companies and also achieve some remedial effect through requiring special review committees and assurances from companies that they had stopped the questionable practices, there was still a strong outcry for a complete prohibition against this bribery in order to restore public confidence in business and in our foreign policy.

Consequently in 1977 both Houses of Congress unanimously passed the Foreign Corrupt Practices Act.

That brings us to the present and the reason we are here today. From the moment the act was passed, it has been attacked as unwarranted interference in a variety of corporate affairs. Moreover, there have been many dire warnings that ultimately it would harm U.S. economic interests abroad.

These voices have grown louder during this Congress. We are being told by business and trade groups that the act is a major disincentive to exports and harmful to our national interests, our balance of trade, and our economy.

No Member of Congress is more convinced about our role in global trade than I am. I am convinced if we are to regain our domestic economic health, we must maintain and enlarge our competitive edge in world markets; in fact, exploring ways to do that is one of the priorities of this subcommittee.

Therefore, before exploring any amendments to modify the act, I think it is appropriate to examine the underlying reasons for the act, its purposes, the conditions it sought to deal with, and the public policy it sought to achieve.

Rather than go roaring in with the perception of a fix for a problem that isn't yet defined, let's first define the problem.

Our goal is to carefully determine whether those purposes and policies have continuing validity. This is the first in a series of oversight hearings which will be followed by an exploration of the manner in which the SEC and the Department of Justice have enforced the act.

We, as a subcommittee, will study how effective the act has been in curbing bribery and how well the two agencies have done their job.

We sent letters to the Department of Justice and the SEC requesting detailed information about cases, investigations, and disclosures under the act. We will take their responses and others into consideration.

We will also be looking at the real impact of the act on foreign trade and exports. Our staff will be working with the staffs of the Departments of State and Commerce and the Office of the Special Trade Representative this week to request and work with them on identifying precisely what may be going on.

After, and only after, this careful and thorough consideration of the history and enforcement and implications of the act will it be possible to consider modifications.

That is how this subcommittee plans to proceed.

We are honored to have a very distinguished and knowledgeable panel this morning, people intimately involved in making the law back in the mid to late 1970's. I think they will make an invaluable contribution to us.

Our first witness this morning who has asked to testify and who will be our lead-off, is the Honorable Robert Eckhardt, a former and very distinguished Member of this Congress, this subcommittee and this committee, and one who is deeply involved with this point.

Robert, welcome back to the Energy and Commerce Committee.

Mr. Collins, would you like to make a statement?

Mr. COLLINS. Thank you, Mr. Chairman.

I am pleased the subcommittee is going to take a look at the Foreign Corrupt Practices Act and consider the policies and the purposes which led to the enactment of this law.

I hope later on we will move to the problems which this statute has caused for American business. It has caused very, very serious problems.

We can make revisions and correct these problems and leave our country in a better position on exports.

I am sure no member of this committee supports bribery of foreign officials. We are concerned about the ambiguity of the statute and the confusion that it has caused for U.S. businesses and the unnecessary burdens it has placed on them.

Earlier this year our subcommittee held a series of hearings on international trade in telecommunications products and services. It has been brought out that we suffer when we try to compete with foreign industry. We have more requirements than the foreign governments have placed on their businessmen to operate.

European and Japanese firms are beginning to challenge U.S. technological leadership all over the world, and they are not subject to similar regulations.

Now, what we need to do is to work out some changes in the law that can clarify it and give our businesses an equal opportunity in the foreign trade of the world today.

Thank you, Mr. Chairman.

Mr. WIRTH. Thank you very much.

Mr. Mottl.

Mr. MOTT. No statement. I just want to welcome Bob Eckhardt, a member we held in great esteem. Welcome, Bob.

STATEMENT OF ROBERT C. ECKHARDT, WASHINGTON, D.C.

Mr. ECKHARDT. Mr. Chairman, thank you.

Thank you all for permitting me to be here. I have a feeling of nostalgia being in this room with old friends and colleagues.

I come here not representing any group, person or corporation. I just represent Bob Eckhardt, a lawyer here in Washington, D.C.

So far as I know, I have no clients who have a particular interest in this act or have shown any interest, but I appear here as, I suppose, the principal author of the act when it was offered, at least in the House of Representatives.

I was very concerned about the act at that time.

As you will remember, several things had happened that very much shook the United States image and position abroad. The Prime Minister of a great nation had fallen due to a bribe in which Lockheed had been engaged; the Prince of The Netherlands, as I recall—I believe that was correct though I am not entirely familiar now with all of the circumstances that occurred during that—but I want to say this: the United States is the greatest trading nation in the world. The United States has a reputation for dealing in commercial matters with a manner of high integrity.

When I was chairman of the Committee on Consumer Protection and Finance, I can recall for the first time being on the floor of the New York Stock Exchange and seeing persons there engaged in transactions that involved millions of dollars in which the entire

gesture which closed the deal was merely a nod, a wave of the hand, the recognition of a person approaching the specialist on the floor.

That is what makes this Nation great. That is what makes trading possible. That is the reason this Nation is the leading trading country in the world.

It is a question of business integrity.

I know it has been said that the United States should be able to, when in Rome, do as the Romans do. Well, I think they can pretty well do as the Romans, but they cannot do as the Borgias used to do.

The act merely provides that there shall not be activities which influence the effect of officials of another nation.

It has absolutely nothing to do with a situation like this. Suppose, for instance, it is difficult to get your goods off the dock because it is customary in that country for whoever is in control of the docking facilities, but who does not make determinations of a policy nature, to receive some sort of a gratuity, mordita, as they call it in Spanish.

I guess almost every nation has a name for it. The act very carefully steered around such propositions. There was one thing that really concerned me very deeply when the act was being drafted: I was fearful that if the act were not carefully drawn, there could be a result in which a person who was working for a large corporation overseas might innocently engage in some activity in which perhaps he paid respects to some official of a foreign country not because he was attempting to bribe that country, but later the matter came into the news and perhaps was embarrassing to the company that employed him.

I was afraid that that company might make him the scapegoat, convict him of an offense, and in that way appear to be completely clean of any offense.

So the act provides that in order for an individual as an agent of a corporation to be held guilty of bribery, that his principal must be involved and must be guilty of the offense.

In that way, of course, Joe Blow, for instance, in Rome, who may have sent a bottle or case of champagne to some official of that country because he was a friend of the family, could not be called up and tried in an American court, a U.S. court, without an opportunity to bring before that court witnesses that could give testimony in excusing him from the act that he was asserted to have engaged in.

I think the act is pretty carefully drawn. I see no reason why the act should be weakened. Of course, it is always true in any criminal act that—or, for that matter, in civil acts as well—that sometimes need interpretation.

I think that the question of mere ministerial or clerical activities pretty well defines what constitutes the mere grease payment.

I am sure nobody is going to say they are for bribery. I doubt anyone will call for the absolute repeal of the act, but there are other methods that are being used these days to undermine what seems to me to be salutary legislation. That is activity which, in effect, prevents the legislation from being enforced or legislation

which so weakens the language when applied by a prosecutor that it becomes virtually impossible to win a case.

I think that this very committee, in its hearings in connection with the violations of the Department of Energy Act, has seen that, where the enforcement agencies of DOE have been greatly reduced in number to the point where perhaps some \$7 billion may go unrecovered by those who were injured.

In many instances the money would ultimately go to the Treasury of the United States in order to save a few million dollars in costs for the prosecutors. I think that is a mistake. I think that this committee needs to be very careful that acts are not either weakened in the enforcement armor in the language of the act itself which would permit effective enforcement.

I know when the act was before Congress the first time we had very few people who said they were against it, but there was a great deal of activity behind the scenes to undermine it.

As a matter of fact, I had the act up one Monday on the suspension calendar when on Thursday I found it had been pulled off. I spoke to the Speaker about it and he said that a gentleman in Boston who was engaged with an accounting firm had indicated that we could not—if this act were passed—trade overseas effectively under it.

The Speaker was a little impressed about that at first, so I went back to the office and called the staff in. We sent this gentleman a telegram saying that we were sorry that he had not come before us when the act was heard the first time, but that we would give him that activity that Saturday and hold a hearing on that Saturday, a rather unusual procedure, I must say, and it might have been rather difficult to carry it off if it went forward.

Fortunately, we did not have to do it. When his principal, the president of a large accounting firm, who was at the time vacationing in Paris, found out about it, he immediately got in touch with him and said, pull that off, quit that, don't fight the Foreign Bribery Act. We don't want to be associated with an opposition to an act prohibiting foreign bribery.

So the bill went back on, on that Monday and was passed on the Suspension Calendar.

Mr. WIRTH. Your position at this point is that this committee ought to look very carefully at the bill, probably not make any changes in the legislation, that the enforcement pieces are right?

Mr. ECKHARDT. Yes, sir, I think that is correct.

Mr. WIRTH. There are a lot of people on the committee and in the Congress now who were not in the Congress during the 1973 to 1977 period, who were not here during the history of the act, nor the passage of the act.

The panel which will follow you is focused on the history of the act, the public policy basis for having the legislation and the accounting requirements that are in the act. It is important that we all understand this thing before getting to any possible changes. I think the minority has agreed with this process.

We certainly look forward to being able to work with you on the history of the act and working through any problems that may exist in the act.

I think Mr. Rinaldo also had a statement that he wants to give. Mr. Rinaldo has been particularly interested in this legislation. He has a statement for the record.

Mr. RINALDO. Yes, I do, Mr. Chairman.

I am sorry I was a few minutes late. We had a Republican conference that I was attending.

As you know, I am the principal sponsor of this bill in the House and I will say, as the gentleman testifying knows, that I was here during all of the previous hearings on the legislation and participated actively in those deliberations.

This morning I want to particularly thank the chairman for conducting these oversight hearings. As our former colleague, Bob Eckhardt, stated a few moments ago, when the act was passed 4 years ago, there was a clear need at that time to set forth in unmistakable terms the policies of our Government regarding the conduct of American companies toward foreign companies.

Revelations at that time of highly improper and illegal conduct involving millions of dollars by large numbers of public companies outraged the public.

As a result, the act, the Foreign Corrupt Practices Act, was unanimously passed by Congress. I strongly supported the act at that time.

I feel very strongly that we must continue to adhere to those policies and to oppose bribery of foreign officials which is objectionable to our country and to those nations with which we do business, but we should and we must return to our goal of clearly setting forth what our Government policy is and what our code of conduct is.

Since the passage of the Foreign Corrupt Practices Act in December 1977, American companies have improved their methods of doing business overseas, have strengthened company codes of conduct for employees, and have instituted a number of far-reaching internal accounting controls.

We have now had time, and it is important to bring this out, to evaluate the Foreign Corrupt Practices Act in terms of real world experience, and that experience has revealed a number of problems with the act.

Therefore, I feel that it is time that Congress took a good hard look at the statute and how it is working.

We need to review its effectiveness in terms of eliminating bribery of foreign officials as well as its effect on the equally important national policy of promoting American business overseas, and this hearing, Mr. Chairman, is what I would hope would be the first step in a thorough review and much needed revision of this statute.

Let me give you an idea of some of the problems which have arisen under the implementation of the act and which make revision desirable.

First of all, uncertainty as to what constitutes a bribe and what is prohibited conduct on the part of American companies operating overseas.

Second, a company's liability for actions of its foreign agents.

Third, the reason to know standard contained in the act.

Fourth, the cost of complying with the accounting and record-keeping requirements which fall on all publicly held companies.

And finally, the split of enforcement authority between the Department of Justice and the SEC which has led to uncertainty about enforcement policies.

That is why I introduced the legislation, the identical bill Senator Chafee has introduced in the Senate, legislation which I hope can be considered by this subcommittee as a basis for revising this statute.

This legislation has been cosponsored by other members of the committee as well as a number of other Members of the entire House.

The requirements of the act and the uncertainties it has created have imposed unnecessary costs and a considerable burden on American companies.

It has resulted in reduced exports and the unwillingness of foreign governments, companies, and agents, to do business with American companies.

The GAO, in a report released earlier this year, found that 30 percent of the firms participating in its survey had lost overseas business as a result of the act. In addition to that GAO study, there have been a number of other studies conducted by the export council and private groups indicating the severe export disincentives caused by the statute.

The administration has indicated that the revision of the Foreign Corrupt Practices Act is a high priority as part of its program to improve the position of the United States in world trade.

The State Department, Justice Department, Commerce Department, Office of the United States Trade Representative, as well as the SEC, have all indicated that changes in the act are necessary.

I would hope that the subcommittee can move expeditiously, Mr. Chairman, with its oversight hearings, with its review of the statute, and get on to consideration of legislation to make these much needed revisions. We need to reconcile the policies and purposes of the act with the need to promote U.S. business abroad.

Finally, what we have to really do is make sure that the Foreign Corrupt Practices Act stops bribery but doesn't stop exports.

Thank you very much, Mr. Chairman.

Once again, thank you for holding what I consider a very, very important hearing so that we can air the problems that American companies are having with this act.

Mr. WIRTH. Thank you, Mr. Rinaldo.

Mr. Collins.

Mr. COLLINS. Thank you, Mr. Chairman. As you welcomed our former colleague, Mr. Eckhardt, to this hearing, I just wanted to add something about Mr. Eckhardt. I served with him many years. I never knew a more brilliant, a more outstanding Member of the House, and I think he will probably go down in history as the most outstanding liberal that ever served from Texas, and maybe the most outstanding that ever served from the South.

I have the deepest admiration for Mr. Eckhardt because in my philosophy I am what you might call a conservative, but very, very objective through the years in seeing Mr. Eckhardt as he spoke on the floor, and as he worked on the committee. In all of my years in Congress I never found anyone who was more articulate, who was

more consistent, who was more dedicated, and who was completely and entirely sincere.

I have seen you cast so many votes which I knew were politically unpopular, but you always voted from the heart. I feel honored that you have come to visit with us again. History will probably prove that you were the greatest liberal that ever came from the South.

Mr. ECKHARDT. I greatly appreciate that compliment from you, Mr. Collins. I am not articulate enough though to have convinced you many times. That speaks well for your own strength of your views and your point of view.

Mr. Chairman, may I comment just briefly on this question of trade, foreign trade?

I just do not believe that there is anything since the passage of the act that indicates any diminution of trade.

Of course, I recognize that there are many things that affected foreign trade like, for instance, the strengthening of the dollar and certain activities that we took with respect to improving our trade abroad, but the act was passed the latter part of 1979.

Trade in Maryland's exports had been, in 1975, \$107.7 billion; 1976, \$115.2 billion; 1977, \$122 billion; in 1978, \$143.7; 1979, \$181.9; 1980, \$220.6. That is Maryland's exports.

About the same figures appear for exports of manufactured goods. There was \$71 billion, \$77 billion, \$80 billion before the passage of the act. After, \$94.5 billion, \$116.7 billion, and \$144 billion in 1980.

Certainly though I do not say that this increase was caused by the act, the act certainly did not impede the trade of the United States which in all of these years with respect to Maryland's exports was ahead of every other country in the world.

Mr. WIRTH. I appreciate that. We will examine the impacts of the act at a later hearing. Again, what we wanted to try to do today was, first, do a background as to why the act exists.

We will be looking forward to talking with you and our staff will be working with State and Commerce and the Office of the Special Trade Representative to identify what the flows of trade have been and to identify where the specific impact of the act, if any at all, have been.

Robert, thank you very much for being with us. We greatly appreciate it and look forward to working with you.

Mr. ECKHARDT. Thank you.

Mr. WIRTH. The remainder of the morning will be focused on a very distinguished panel of witnesses, and I hope you could all join us at the witness table at this point.

We have Mr. Irving Pollack, former Commissioner of the Securities and Exchange Commission, who will be the leadoff member of the panel.

Second, Mr. Rod Hills, former chairman of the SEC, and an attorney here in Washington.

Third, Dr. Marshall Clinard, distinguished research professor of sociology at the University of New Mexico.

Fourth, Hon. James Akins, former U.S. Ambassador to Saudi Arabia, and finally, Mr. Jack Blum, former counsel to the Senate Subcommittee on Multinational Corporations.

STATEMENTS OF IRVING M. POLLACK, WASHINGTON, D.C.; ROD-
ERICK M. HILLS, WASHINGTON, D.C.; MARSHALL B. CLINARD,
PROFESSOR OF SOCIOLOGY, UNIVERSITY OF NEW MEXICO;
JAMES E. AKINS, WASHINGTON, D.C.; AND JACK A. BLUM, WASH-
INGTON, D.C.

Mr. POLLACK. Thank you, Mr. Chairman.

Mr. WIRTH. Gentlemen, I think you got a sense of what we are trying to do. I think it is important to review where the act came from and why. That is the purpose of these hearings.

We will then follow it up with specific comments on the impact of the legislation.

We will include your statements in full in the record. I hope we can summarize your statements and then we will conduct an exchange between members of the panel and the members of the subcommittee.

Mr. COLLINS. Before they start, Mr. Chairman, I would like to repeat, I hope they can condense their statements.

I ask unanimous consent that their full statement be included in the record.

Mr. WIRTH. That will be done, without objection.

Mr. Pollack.

Mr. POLLACK. Mr. Chairman, I think that Mr. Eckhardt and the committee referred to the conditions that led to the passage of the Foreign Corrupt Practices Act of 1977.

What I would like to do is go back and give you the impression that the Securities and Exchange Commission had which led to its recommendations to the Congress and the ultimate inclusion of the accounting provisions in that act.

First, it is important to note that our financial and security markets which are the best in the world depend heavily upon the confidence of investors in the Federal securities disclosure program.

The disclosures program is at the heart of the securities market. Without investor confidence, I think it is fair to state that our market would not maintain its position as the leading capital market in the world.

I think that the introduction to the report which the Commission submitted to the Congress and which Chairman Hills was responsible for authoring summarizes perhaps best the ultimate finding of the Commission from the investigations which it conducted into the so-called questionable payments in the mid-1970's.

In that 1976 report to the Congress, the Commission observed:

The almost universal characteristic of the cases reviewed to date by the Commission has been the apparent frustration of our system of corporate accountability which has been designed to assure that there is a proper accounting of the use of corporate funds and that documents filed with the Commission and circulated to shareholders do not omit or misrepresent material facts. Millions of dollars of funds have been inaccurately recorded in corporate books and records to facilitate the making of questionable payments. Such falsification of records has been known to corporate employees and often to top management but often has been concealed from outside auditors and counsel and outside directors.

In light of the magnitude of the problem, the Commission did two things, broadly speaking. One was to bring actions against firms that had engaged in these payments and require remedial action in the form of special committees which hired accountants

and lawyers to make a special investigation in the questionable payments area, to make a report to their boards, so that appropriate corrective action could be taken.

In addition, because of the scope of the problem, the Commission, through its representatives, suggested to the corporate community that a voluntary disclosure program in this area would be in order, set forth various conditions for that, and encouraged well over 300 companies to come forward and disclose these questionable payments.

I emphasize that the Commission's program was not to punish, but to strengthen the corporate system in this country by removing the conditions that had led to serious concern with corporate accountability.

As a result of the Commission's actions, codes of conduct were established by many corporations.

In addition, special audit committees were set up to make certain that the corporation's business was being reflected honestly and conducted honestly.

The Commission, of course, was not interested in conducting a worldwide morality campaign, but I hasten to add that I don't think the fact that the program of the Commission was consistent with good morals should be something that we should be ashamed of or considered to be detrimental.

While the Commission was conducting its investigations, there was increasing concern in the Congress, as has already been indicated, in view of the detrimental events that were taking place in some of the foreign countries as a result of these disclosures; and so the congressional hearings, while they dealt with the accounting provisions, also picked up the question of the antibribery legislation that the Congress thought as a matter of international and national policy was appropriate.

The Commission's concern, of course, from its own jurisdiction was with respect to the operation of the corporations and their disclosures, and in that regard the Commission recommended to the Congress, among other things, two basic provisions, very simple provisions which any corporation, in order to conduct a proper business, must have:

First, that the corporation should maintain books which give reasonable assurance that they are adequate and accurate with respect to accounting for the corporation's assets and operations.

Second, that the internal controls of the corporation intended to make certain that the corporations activities are properly conducted should be strengthened to make sure that there was proper corporate accountability.

These were the two major recommendations of the Commission to the Congress and were ultimately included in the legislation that became the Foreign Corrupt Practices Act of 1977.

With respect to the bribery position, the Commission believed that that was a matter for the Congress in view of the international and other national policies beyond its own jurisdiction.

As a personal comment, I would just like to make two points: During my tenure as a Government official, I dealt with numerous Government officials in other countries who were conducting the same sort of regulatory oversight that we were at the Commission

here in the United States, and as I thought about the question of bribery and other corrupt payments, it occurred to me that it would have been very difficult for me to have established and maintained the confidence that we had with those officials if our agency or I had been aware of corrupt payments being made by U.S. corporations and we had not brought that to their attention.

In addition, in the course of my travels, I have become increasingly aware of the fact that our adversaries around the world use propaganda to attack our free enterprise and democratic system on the basis of many unfounded statements. I think it would be unfortunate for us to condone bribery or other similar conduct which would give some support to the propaganda which is already being extensively put forth in the international community in an effort to undermine our democratic and free enterprise system.

Thank you.

[Mr. Pollack's prepared statement follows:]

STATEMENT OF

IRVING M. POLLACK

Today's session is directed to the factors which led to the enactment of the Federal Corrupt Practices Act of 1977 ("FCPA") and the purposes and goals of that Act. Before addressing those subjects, a few brief observations are in order to place that discussion in context.

Fundamental to a viable and strong capital market is confidence of investors not only in the fairness of the market system, but also in the truthfulness of the information disseminated concerning the issuers whose securities are traded therein.

The U.S. securities markets - at least in part - gained and maintain their superiority over all others in the world, because of our federal securities disclosure system. Broad institutional and individual participation, both nationally and internationally, in our securities markets in large measure is based on the honesty of the reporting system and worldwide confidence in it. Fundamental to this confidence is the integrity of management and reliability of corporate books and records.

The Securities and Exchange Commission's investigations of questionable and corrupt payments in the mid-1970's disclosed that a large number of U.S. corporations - including some of the largest and most respected - engaged in illicit payments to a surprising extent. Hundreds of millions of dollars were paid out, particularly to foreign officials, by over 450 companies. These disclosures came as a surprise to both the private as well as the public sector.

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For the Commission it presented a critical problem. It indicated a breakdown in corporate accountability and disclosure, which if not corrected, could undermine the basic underpinnings of corporate accountability and the disclosure system. The failure of the companies to report these illicit payments, and the circumstances under which they were made, rendered false and misleading their financial reports and other representations concerning the method by which they managed and conducted their business. It also placed in serious jeopardy their foreign assets and operations.

It further reflected significant deficiencies in internal controls and inadequacies and inaccuracies in basic company documents and records.

As the Commission emphasized in its 1976 Report to the Congress:

"The almost universal characteristic of the cases reviewed to date by the Commission has been the apparent frustration of our system of corporate accountability which has been designed to assure that there is a proper accounting of the use of corporate funds and that documents filed with the Commission and circulated to shareholders do not omit or misrepresent material facts. Millions of dollars of funds have been inaccurately recorded in corporate books and records to facilitate the making of questionable payments. Such falsification of records has been known to corporate employees and often to top management, but often has been concealed from outside auditors and counsel and outside directors."

The Commission recognized that because of the magnitude of the problem a broad remedial program was needed

to correct the situation. This was its objective throughout the period of its investigations. It primarily was interested in reestablishing corporate responsibility and not in punishment. Accordingly, in addition to its enforcement actions, the Commission promoted and encouraged a voluntary disclosure program by issuers of questionable or illegal foreign payments.

In its court actions the Commission sought and obtained permanent injunctions prohibiting future violations involving similar conduct. These decrees also required companies to establish special review committees comprised of independent directors to conduct full investigations of the misconduct charged by the Commission. To assist them, the Committees generally retained independent accountants and special counsel to make thorough inquiries, including intensive examinations of the books and records of the companies. Reports and recommendations of the special committees were required to be submitted to the boards of directors for review and implementation.

In addition to specific corrective measures, many companies established codes of conduct for their personnel, set up independent audit committees and took other actions designed to prevent such conduct from occurring in the future.

The Commission was not interested in a worldwide morality campaign. It was interested in ensuring that U.S. issuers were acting responsibly and honestly, so that investors could rely with confidence on their representations as

to the quality of their earnings, the quality of their services, products and business, the quality of their management and in short their ability to compete effectively in a free enterprise system.

Concomitantly with the Commission's investigations and actions, Congressional committees were engaged in their own hearings and inquiries. For as the Commission noted in its 1976 Report, "The question of illegal or questionable payments is a matter of national and international concern . . ." The Congress was increasingly troubled not only by the impact on the securities markets, but also with the harm that such payments had done to our international relations and the damaged U.S. business image it had created at home and abroad.

The Commission further emphasized in its 1976 Report that, "Whatever their origin, the Commission regards defects in the system of corporate accountability to be matters of serious concern. Implicit in the requirement to file accurate financial statements is the requirement that they be based on adequate and truthful books and records. The integrity of corporate books and records is essential to the entire reporting system administered by the Commission." And in its comments on proposed legislation to deal with the problem, the Commission added:

[W]e believe that any legislation in this area should embody a prohibition against the falsification of corporate accounting records. The most devastating disclosure that we have uncovered in our

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recent experience with illegal or questionable payments has been the fact that, and the extent to which, some companies have falsified entries in their own books and records. A fundamental tenet of the recordkeeping system of American companies is the notion of corporate accountability. It seems clear that investors are entitled to rely on the implicit representations that corporations will account for their funds properly and will not "launder" or otherwise channel funds out of or omit to include such funds in the accounting system so that there are no checks possible on how much of the corporation's funds are being expended or whether in fact those funds are expended in the manner management later claims.

* * * *

[A]ny legislation should require management to establish and maintain its own system of internal accounting controls designed to provide reasonable assurances that corporate transactions are executed in accordance with management's general or specific authorization; and that such transactions as are authorized are properly reflected on the corporation's books and records in such a manner as to permit the preparation of financial statements in conformity with generally accepted accounting principles or any other criteria applicable to such statements.

The concept of internal accounting controls is not new. It has been recognized by the accounting profession as being an important responsibility of management. * * * *

In summary, the objective of the accounting provisions of the FCPA, which require issuers "to make and keep books, records and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer; and * * * to devise and

maintain a system of internal accounting controls sufficient to provide reasonable assurance that - transactions are executed * * *" pursuant to proper authorization, are appropriately recorded to permit preparation of proper financial statements and to provide proper accountability for and control over assets, were designed and intended to strengthen corporate accountability and restore the integrity of the corporate disclosure system.

The anti-bribery provisions of the FCPA, according to the Congressional Reports, were designed and intended to eliminate corrupt practices which the Congress found were destabilizing and detrimental to the long-run interests of American business and U.S. foreign relations and inconsistent with the basic underlying principle of our free enterprise system that businesses should prosper on the basis of superior performance and not by corrupting activities.

In determining what legislation was appropriate for dealing with "bribery", as such, the Commission recognized that this was a question of national policy for the Congress to consider in the larger context of our international relationships.

However, I should add as a personal note and observation, that as a government official, I had personal dealings with a number of foreign officials performing similar functions to mine in their countries. I do not think I could have established and maintained the mutual confidence and cooperation required for proper oversight of

today's securities markets, if it turned out that my agency and I were aware that U.S. companies were bribing their associates or subordinates and I did not bring it to their attention.

Also, there is sufficient propaganda spread by our adversaries about how our capitalistic society purportedly operates, without our condoning the conduct of our corporate officials which undermines our claim that our economic success is based on our superior efficiency in productivity, the quality and price of our products and services with our companies fairly and honestly competing in a free enterprise system.

Finally, the fact that the SEC's disclosure program and requirements also happened to be consistent with good moral principles, certainly was and is not something to be ashamed of or detrimental. But, I emphasize again that the Commission's actions and program were confined to its statutory jurisdiction and responsibilities.

I shall be pleased to answer any questions the Committee may have.

Mr. WIRTH. Thank you very much, Mr. Pollack.
Mr. Hills?

STATEMENT OF RODERICK M. HILLS

Mr. HILLS. Thank you, Mr. Chairman.

I have little to add to Mr. Pollack's comments except to note that in the hundreds of cases considered by the Securities and Exchange Commission in the period of 1975, say, through 1980, there were many different types of conduct which are very hard to characterize under any one category.

Certainly there were some gross examples of behavior which by any standard could be reprehensible. There was certainly a good deal of evidence of the arrogant use of corporate assets for personal use, such as expense accounts.

There was some plain carelessness, some childishness in terms of kind of boyish intrigue. People like to have agents abroad, and secret bank accounts; maybe a common human behavioral characteristic that some people like to act secretly and do things in a way which no one else can supervise them.

In those gross cases I mentioned, it was fairly easy for anyone to pass a moral judgment, but in the vast majority of the cases, reasonable men could and did differ as to whether or not the act or the conduct was in some ultimate sense immoral, improper, wrong.

The grace of the activities of the Commission was that we did not have to pass a moral judgment. The one common feature to the cases in which the SEC found error was that the system, as Mr. Pollack said, of corporate accountability had broken down.

A common theme was the actions had been taken without the semblance of corporate authorization: Outside the spotlight of the outside auditors, outside the purview of the outside counsel, without the attention of the outside directors—assuming that there were any outside or independent directors on the boards of these publicly held companies.

In response to what the Commission found, the Commission filed a report in which we all participated at great length which I commend to this subcommittee as the basis for beginning your examination of the roots of the FCPA.

For in that report I think we found the characteristics that were common to the cases that followed as well as those that came before the report. What we said in that report, indeed, what we did not say in that report, may be of some significance and should be, in my judgment, of some significance to this committee.

We said that once we found this behavior, this action without corporate authorization, the Commission was fully enabled, fully empowered to deal with it.

We didn't seek any more penalties. We didn't seek any more punitive powers. We saw no inadequacy of the actions that were taken by the SEC when we found something wrong.

What we did say was that we did not find them often enough, that the system of internal controls had broken down.

So we did essentially ask more than anything else for an endorsement of what we thought might have been our authority anyway, but we sought congressional endorsement for the right of

the Commission to require controls adequate for the proper corporate governance of the actions of the employees; controls that could be submitted to outside auditors for scrutiny and which would provide a chance for outside directors to deal with it.

Of course, without independence, without an independent character on the boards of directors of our large multinational companies, whatever controls we might have had would have been inadequate.

We made an effort, a gesture, a request to the private sector, primarily to the New York Stock Exchange, to see whether or not it wasn't time that a standard of independence be created on the boards of directors of the companies.

We were gratified at the time that the New York Stock Exchange moved promptly in response to the request that I made on behalf of the Commission in my letter to the chairman of the New York Stock Exchange to ask that independent audit committees be created on the boards of all New York Stock Exchange companies.

I am pleased to say today that it is rare—certainly any large multinational company—it does not happen that there is not a truly independent character on the boards of those companies that interact with the newly established internal controls.

We also went to the auditing profession and said your standards of conduct are inadequate. You have not established a sufficiently precise standard for your auditors when they uncover something that seems suspiciously beyond the normal realm of corporate activity.

Too often an auditor was willing to accept the word of someone: "Well, that was all right"; "that was authorized"; "that was proper"; then made a note in his own book and would pass on.

So at our request, the auditing profession, the American Institute of Certified Public Accountants, their executive committee established a new auditing standard which said in the colloquial, if you see something suspicious, you better make sure somebody with authority hears about it.

Of course, if that was top management, there had to be an independent element that the outside auditors could go to.

So a system of corporate governance responsive to the problem we found has evolved. The things the SEC thought should be done to meet the problem that the SEC saw back in the midseventies was well established by 1977 and one of those steps was, of course, the accounting provisions of the FCPA.

If I may only depart from the assigned topic of the day to say this, there were many in the Nation and many in the Congress that felt something more needed to be done, something more than the Securities and Exchange Commission asked for; something had to be done with respect to the morality of what had been seen.

So a judgment was passed and an assumption was made that all of this conduct, all of these things that we had seen in so many cases which had such a dramatically different quality to them could somehow be characterized as legal or illegal and a criminalization occurred and an attempt to regulate the activity by criminal laws was added to a system which attempted to cause a disclosure of the activities.

My own judgment and the long history and the great success of the Securities and Exchange Commission has been that disclosure

is the best disinfectant and moral judgments can be left to the people once they see what in fact happened.

My own judgment is that the system in place, without the criminalization, is what has caused a dramatic change in corporate behavior in America.

My own judgment is that the unnecessary criminalization, the unnecessary attempt to pass moral judgment on so many acts of so many different varying characteristics has placed an undue burden on corporate officials, on the audit committees on which I sit, the three major audit committees which I chair, it has made it far too difficult for us to make the kinds of business judgments that we would be free to make in a public arena. Of course, with new internal accounting rules, it has also made it far too difficult for the accounting firms to decide what kind of internal controls there should be.

My own suggestion is that this subcommittee seriously consider a significant reduction in the criminal penalties. It may very well be that the accounting provisions do need some amendment, but I think the lack of pressure from criminalization would make the accounting rules much more understandable to the business profession and to the accounting profession. Then this subcommittee could urge the Government to engage in something that has not been attempted, namely, very serious bilateral negotiations with our trading partners to attempt the same type of discovery, same type of corporate reporting we have managed so well in this country.

Thank you.

[Testimony resumes on p. 48.]

[Mr. Hill's prepared statement and attachment follow:]

STATEMENT OF
RODERICK M. HILLS

I AM PLEASED TO HAVE THIS OPPORTUNITY TO OFFER MY VIEWS ON THE PURPOSES AND GOALS OF THE FOREIGN CORRUPT PRACTICES ACT. THE SUBCOMMITTEE IS TO BE COMPLIMENTED ON EMPHASIZING THE NEED TO REEXAMINE THOSE CORPORATE ACTIVITIES THAT GAVE RISE TO THE PASSAGE OF THE ACT. FRANKLY, I BELIEVE THAT FAR MORE TIME SHOULD HAVE BEEN DEVOTED TO THE SAME SUBJECT BEFORE ITS PASSAGE. THE RESULT, I BELIEVE, WOULD HAVE BEEN BETTER LEGISLATION, LEGISLATION THAT WOULD NOT HAVE CAUSED THE CONFUSION AND CONCERN THAT HAS EXISTED IN THE CORPORATE WORLD THESE PAST FOUR YEARS, AND LEGISLATION THAT WOULD NOT NOW BE IN SUCH CLEAR NEED OF AMENDMENT.

I ASSUME YOUR INTEREST IN MY VIEWS STEMS LARGELY FROM MY TERM AS CHAIRMAN OF THE SECURITIES & EXCHANGE COMMISSION FROM 1975 TO 1977, THE PERIOD IN WHICH THE PROBLEM OF CORPORATE QUESTIONABLE PAYMENT BECAME APPARENT. THIS SUBCOMMITTEE SHOULD KNOW, HOWEVER, THAT FROM 1971-1975 I SERVED AS CHAIRMAN OF A NEW YORK STOCK EXCHANGE CORPORATION THAT FACED THE KINDS OF PROBLEMS NOW SUBJECT TO THE FOREIGN CORRUPT PRACTICES ACT AND THAT I NOW SERVE AS CHAIRMAN OF THE AUDIT COMMITTEES OF THREE LARGE INTERNATIONAL COMPANIES THAT MUST NOW DEAL WITH THE FCPA.

IN THE SPRING OF 1976, AT THE REQUEST OF SEVERAL COMMITTEES OF THE CONGRESS, THE SEC ORDERED A COMPLETE REVIEW OF ALL OF THE SO-CALLED QUESTIONABLE PAYMENT CASES THAT HAD BEEN INVESTIGATED BY THE SEC AND I SUPERVISED THE PREPARATION OF A COMPREHENSIVE REPORT THAT SET FORTH:

WHAT WE HAD FOUND,

WHAT THE SEC PLANNED TO DO IN THE FUTURE, AND

LEGISLATION WE THOUGHT WOULD BE APPROPRIATE.

I SUGGEST THAT THIS SUBCOMMITTEE RESTUDY THAT REPORT, FOR IN RETROSPECT I FEEL GOOD ABOUT WHAT WE SAID THEN AND CLEAR ABOUT WHAT SHOULD BE DONE NOW.

IN THAT REPORT, WE STATED THAT THREE CONSIDERATIONS

SHOULD BE PARAMOUNT TO CONGRESSIONAL CONSIDERATION OF THE CORPORATE QUESTIONABLE PAYMENT ISSUE.

FIRST, WE REPORTED THAT THE COMMISSION HAD DEALT EFFECTIVELY WITH QUESTIONABLE CORPORATE PAYMENTS UNDER LAWS THEN EXISTING. WE SAID WITH EMPHASIS THAT THE COMMISSION HAD SUFFICIENT AUTHORITY TO DEAL EFFECTIVELY WITH THE PROBLEMS WHEN THEY WERE BROUGHT TO THE COMMISSION'S ATTENTION.

SECOND, WE POINTED OUT, AND I QUOTE FROM EARLIER TESTIMONY, THAT SOMETHING WAS MISSING:

WHAT (OUR) EXPERIENCE HAS TOLD US . . .
IS . . . THAT OUR PRESENT SYSTEM DOES
NOT BRING (SUFFICIENT NUMBERS OF) THESE
CASES TO OUR ATTENTION.

TO REMEDY THAT DEFICIENCY, WE REQUESTED (AND I QUOTE AGAIN):

LEGISLATION TO REQUIRE THAT CORPORATIONS ESTABLISH INTERNAL CONTROLS THAT REASONABLY ASSURE THE PROPER IDENTIFICATION OF FINANCIAL TRANSACTIONS. (EMPHASIS ADDED.)

THIRD, HAVING STRESSED THE NEED FOR IMPROVED INTERNAL ACCOUNTING CONTROLS, WE NOTED A PRESSING NEED TO CREATE A "TRULY INDEPENDENT CHARACTER" ON THE BOARDS OF DIRECTORS OF OUR LARGE COMPANIES, PARTICULARLY THOSE THAT DO INTERNATIONAL BUSINESS. OUR POINT, WAS THAT A NEW FORM OF CORPORATE GOVERNANCE HAD TO EVOLVE: ONE THAT PLACED NEW EMPHASIS ON INTERNAL CONTROLS AND ONE THAT CREATED A SURVEILLANCE OF THOSE CONTROLS THAT WAS INDEPENDENT OF CORPORATE MANAGEMENT. WITHOUT SUCH INDEPENDENT SCRUTINY WE WOULD LEAVE THE "FOX IN CHARGE OF THE CHICKEN COOP." MANAGEMENT, NOT ACCOUNTABLE TO INDEPENDENT DIRECTORS, COULD BE TOO EASILY TEMPTED TO ENGAGE IN QUESTIONABLE PRACTICES, PARTICULARLY IN FOREIGN COUNTRIES, TO IMPROVE CORPORATE PROFITS.

TO PROMOTE THAT "NEW EMPHASIS" ON CORPORATE GOVERNANCE WE APPEALED BOTH TO THE NEW YORK STOCK EXCHANGE AND TO THE AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS ("AICPA").

WE (THE COMMISSIONERS OF THE SEC) MET FIRST WITH THE AICPA. WE ASKED ITS AUDITING STANDARDS EXECUTIVE COMMITTEE ("AUNSEC") TO ESTABLISH BETTER DEFINED RULES TO DEAL WITH SUSPICIOUS ENTRIES THAT WERE OBSERVED IN THE COURSE OF THE ANNUAL AUDITING OF CORPORATE BOARDS BY INDEPENDENT AUDITORS. REPEATEDLY WE HAD REVIEWED CASES IN WHICH CORPORATE PAYMENTS WERE QUESTIONED BY OUTSIDE AUDITORS WHO DROPPED THEIR INQUIRIES WHEN TOLD BY THEIR MANAGEMENT CONTACT THAT THE PAYMENT WAS PROPER. FROM MY OWN PRIOR EXPERIENCE AS A CORPORATE OFFICER AND MY OBSERVATIONS AT THE SEC, I CONCLUDED THAT MANY, PERHAPS MOST, AUDITORS BELIEVED THEY HAD NO OBLIGATION TO DO MORE THAN RAISE QUESTIONS WITH WHATEVER CORPORATE OFFICIAL SERVED AS THEIR CONTACT. THE POSSIBILITY THAT SUCH AN OFFICIAL MIGHT HAVE HAD AN ULTERIOR MOTIVE IN SAYING A "SUSPICIOUS" PAYMENT WAS FULLY AUTHORIZED, WAS OF LITTLE OR NO RELEVANCE TO THE AUDIT.

ACCORDINGLY, WE ASKED AUNSEC TO MAKE IT CLEAR THAT AUDITORS MUST DO MORE! IF SOMETHING OF A QUESTIONABLE NATURE WAS SEEN DURING AN AUDIT -- AN UNEXPLAINED COMMISSION, A LARGE "FINDERS FEE," OR AN OFFBOOK SLUSH FUND -- THE AUDITOR WOULD HAVE A PROFESSIONAL RESPONSIBILITY TO BRING THE MATTER TO THE ATTENTION OF SOMEONE OF SUFFICIENT AUTHORITY IN THE CORPORATION TO INSURE AN EFFECTIVE INQUIRY. THUS, IF SOME PAYMENT OF A QUESTIONABLE NATURE WAS SEEN THAT WAS AUTHORIZED BY TOP MANAGEMENT, OUR REQUEST MEANT THAT THE OUTSIDE AUDITOR WOULD HAVE AN OBLIGATION TO BRING THE MATTER TO THE ATTENTION OF THE BOARD OF DIRECTORS.

THE AICPA'S EXECUTIVE COMMITTEE RESPONDED FAVORABLY AND IN 1976 THEY PROPOSED THE FOLLOWING NEW AUDITING STANDARD:

(T)HE AUDITOR SHOULD BE AWARE OF THE IMPORTANCE OF MANAGEMENT'S INTEGRITY TO THE EFFECTIVE OPERATION OF INTERNAL ACCOUNTING CONTROL PROCEDURES AND SHOULD CONSIDER WHETHER THERE ARE CIRCUMSTANCES THAT MIGHT PREDISPOSE MANAGEMENT TO MISSTATE FINANCIAL STATEMENTS.

. . .

IF THE INDEPENDENT AUDITOR'S EXAMINATION CAUSES HIM TO BELIEVE THAT MATERIAL ERRORS OR IRREGULARITIES MAY EXIST, HE SHOULD CONSIDER THEIR IMPLICATIONS AND DISCUSS THE MATTER AND THE EXTENT OF ANY FURTHER INVESTIGATION WITH AN APPROPRIATE LEVEL OF MANAGEMENT THAT IS AT LEAST ONE LEVEL ABOVE THOSE INVOLVED. IF AFTER SUCH DISCUSSIONS THE AUDITOR CONTINUES TO BELIEVE THAT MATERIAL ERRORS OR IRREGULARITIES MAY EXIST, HE SHOULD DETERMINE THAT THE BOARD OF DIRECTORS OR ITS AUDIT COMMITTEE IS AWARE OF THE CIRCUMSTANCES. ALSO, HE SHOULD ATTEMPT TO OBTAIN SUFFICIENT EVIDENTIAL MATTER TO DETERMINE WHETHER IN FACT MATERIAL ERRORS OR IRREGULARITIES EXIST AND, IF SO, THEIR EFFECT.

* * *

WHEN THE AUDITOR'S EXAMINATION INDICATES THE PRESENCE OF ERRORS OR POSSIBLE IRREGULARITIES, AND THE AUDITOR REMAINS UNCERTAIN ABOUT WHETHER THESE ERRORS OR POSSIBLE IRREGULARITIES MAY MATERIALLY AFFECT THE FINANCIAL STATEMENTS, HE SHOULD QUALIFY HIS OPINION OR DISCLAIM AN OPINION ON THE FINANCIAL STATEMENTS AND, DEPENDING ON THE CIRCUMSTANCES, CONSIDER WITHDRAWING FROM THE ENGAGEMENT, INDICATING HIS REASONS AND FINDINGS IN WRITING TO THE BOARD OF DIRECTORS. IN SUCH CIRCUMSTANCES, THE AUDITOR MAY WISH TO CONSULT WITH HIS LEGAL COUNSEL.

OBVIOUSLY, OUR SUGGESTION FOR THIS NEW AUDITING STANDARD WOULD HAVE BEEN OF LITTLE UTILITY IF BOARDS OF DIRECTORS DID NOT HAVE INSTITUTIONAL MECHANISMS FOR RECEIVING COMMENTS FROM THE OUTSIDE AUDITORS, AND IF THESE BOARDS DID NOT HAVE SUFFICIENT INDEPENDENCE FROM MANAGEMENT TO CONSIDER SUCH COMMENTS WHEN THEY REFLECTED UPON MANAGEMENT CONDUCT. ACCORDINGLY, ON MAY 11, 1974, IN MY CAPACITY AS CHAIRMAN OF THE SEC, I WROTE THE CHAIRMAN OF THE NEW YORK STOCK EXCHANGE AS FOLLOWS:

THE EXISTENCE OF AN AUDIT COMMITTEE
THAT MEETS PRIVATELY WITH THE OUTSIDE

AUDITORS TO DISCUSS THE SCOPE OF THE AUDIT, QUESTIONS ARISING DURING THE AUDIT, INCLUDING DISPUTES WITH MANAGEMENT, AND THAT HAS ACCESS TO THE CORPORATE FINANCIAL INFORMATION, IS AN IMPORTANT PART OF OUR EFFORT TO MAINTAIN THE CREDIBILITY OF OUR SYSTEM OF CORPORATE SELF REGULATION. (EMPHASIS SUPPLIED.)

I FURTHER POINTED OUT THE EFFORT TAKING PLACE AT THE AICPA:

I AM SURE YOU ARE AWARE OF THE FACT THAT THE AUDITING STANDARDS EXECUTIVE COMMITTEE OF THE A.I.C.P.A. HAS CIRCULATED AN EXPOSURE DRAFT OF A NEW AUDITING STANDARD WHICH, IF ADOPTED, WOULD REQUIRE AUDITORS TO BRING ANY QUESTIONABLE PAYMENTS THAT THEY MAY FIND TO THE ATTENTION OF A LEVEL OF MANAGEMENT HIGH ENOUGH FOR CORRECTIVE STEPS TO BE TAKEN. IF QUESTIONABLE PAYMENTS BY TOP MANAGEMENT ARE DISCOVERED, SUCH AN APPROACH WILL, OF COURSE, BE ENHANCED IF AN AUDIT COMMITTEE IS IN EXISTENCE.

THE NEW YORK STOCK EXCHANGE REACTED IN SEPTEMBER 1976 WITH A PROPOSAL TO ITS LISTED COMPANIES FOR AN AUDIT COMMITTEE REQUIREMENT. THEREAFTER, THE EXCHANGE FORMALLY PROMULGATED A RULE REQUIRING LISTED COMPANIES TO HAVE SUCH AUDIT COMMITTEES.

I HAVE ATTACHED COPIES OF MY CORRESPONDENCE WITH THE NEW YORK STOCK EXCHANGE IN 1976 AS AN EXHIBIT TO MY PREPARED TESTIMONY.

THEREAFTER, AUDSEC ADOPTED THEIR NEW AUDITING STANDARD; AND THE NEW YORK STOCK EXCHANGE ESTABLISHED, AS A CONDITION OF LISTING, THE REQUIREMENT THAT ALL COMPANIES HAVE AN AUDIT COMMITTEE, INDEPENDENT OF MANAGEMENT, CAPABLE OF PROTECTING THE INTEGRITY OF THE AUDIT PROCEDURE.

ABOUT ONE YEAR LATER, THE FOREIGN CORRUPT PRACTICES ACT WAS ADOPTED. PART OF THAT ACT, THE ONLY PART THAT THE SEC REQUESTED IN 1976, GAVE THE SEC AUTHORIZATION TO REQUIRE ADEQUATE INTERNAL AUDITING CONTROLS.

THUS, BY EARLY 1977, ALL THE STEPS THOUGHT NECESSARY BY THE SEC WERE ENTIRELY IN PLACE. AS A RESULT OF THESE THREE ACTIONS, BY THE AUDITING PROFESSION, BY THE NEW YORK STOCK EXCHANGE, AND BY THE CONGRESS, IN ESTABLISHED NEW CONTROLS OVER THE INTERNAL AUDIT, A VERITABLE REVOLUTION OCCURRED IN THE MANNER IN WHICH OUR MAJOR CORPORATIONS ARE GOVERNED. TODAY IT IS A COMMONPLACE OCCURRENCE FOR AUDIT COMMITTEES TO QUESTION MANAGEMENT IN THE BOARDROOM, WHEREAS SUCH CHALLENGES WERE RARE EVEN SIX YEARS AGO.

ON JANUARY 14, 1976, ON BEHALF OF THE SEC, I MADE THE FOLLOWING OBSERVATION TO THE JOINT ECONOMIC COMMITTEE OF THE CONGRESS:

IN MY VIEW, AN EFFECTIVE SYSTEM OF CORPORATE ACCOUNTABILITY REQUIRES THAT FACTS PERTAINING TO ILLEGAL PAYMENTS NOT BE CONCEALED FROM A CORPORATION'S INDEPENDENT ACCOUNTANT OR ITS BOARD OF DIRECTORS. . . . NOTHING ELSE IN THE SYSTEM WILL WORK UNLESS THE BOOKS AND RECORDS ARE KEPT IN GOOD FAITH.

IT IS MY VIEW TODAY THAT ENORMOUS STRIDES HAVE BEEN MADE IN CREATING AND MAINTAINING A NEW INTEGRITY IN THE BOOKS AND RECORDS OF PUBLICLY HELD CORPORATIONS BY REASON OF THE ACTION TAKEN TO WHICH I HAVE REFERRED, A PROCESS OF IMPROVEMENT THAT STILL CONTINUES AT A GOOD PACE.

TODAY AN INDEPENDENT AUDIT COMMITTEE IS BECOMING A FIXTURE ON THE BOARDS OF ALL PUBLICLY TRADED COMPANIES, NOT MERELY THOSE WHOSE STOCK IS TRADED ON THE NEW YORK STOCK EXCHANGE. NOW THAT A TRULY INDEPENDENT CHARACTER HAS BEEN INJECTED INTO OUR LARGE CORPORATIONS, THAT INDEPENDENCE IS BEING EXPRESSED IN MANY OTHER WAYS: ON "NOMINATING COMMITTEES, COMPENSATION COMMITTEES, AND EVEN 'PUBLIC POLICY' COMMITTEES."

NO DOUBT MUCH MORE NEEDS TO BE DONE, BUT UNTIL THE PRESENT IMPETUS FOR CHANGE HAS SLACKENED, THERE SURELY IS NO NEED FOR FURTHER STIMULUS FROM THE GOVERNMENT. MY POINT IS THAT THE ACTIONS I DESCRIBE WERE DESIGNED TO MEET AND DID MEET THE PROBLEMS WHICH WERE UNCOVERED BY THE SEC.

UNFORTUNATELY, HOWEVER, MANY IN THE NATION AND IN THE CONGRESS FELT THAT IT WAS NECESSARY TO DO MORE. THUS, THE CONGRESS IN THE FCPA WENT ON TO CREATE NEW FEDERAL CRIMES TO REGULATE AND RESTRICT RATHER THAN ONLY TO DISCLOSE QUESTIONABLE CORPORATE CONDUCT. MY PERSONAL OPINION IS THAT THIS CRIMINALIZATION OF THE ISSUE WAS ONE STEP TOO FAR AND THAT THE WHOLE PROGRAM IS NOW SUSPECT BECAUSE CONGRESS DID GO A BIT TOO FAR.

YOU DO NOT NOW SEEK COMMENTS ON HOW THE FCPA HAS BEEN ADMINISTERED AND HOW IT SHOULD BE AMENDED. NONETHELESS, IN YOUR EXAMINATION OF THE FACTS THAT GAVE RISE TO THE FCPA, YOU MAY WISH TO ASK WHETHER THE ORIGINAL LEGISLATIVE REQUESTS OF THE SEC WERE SUFFICIENTLY RESPONSIVE TO THE PROBLEMS FOUND BY THE SEC.

LET ME CONCLUDE, BY RETURNING TO MY THEME. THE ENFORCEMENT PROGRAM OF THE SEC ASSISTED BY THE NEW AUDITING STANDARDS OF THE ACCOUNTING PROFESSION AND THE DEVELOPMENT OF A TRULY INDEPENDENT ELEMENT ON THE BOARDS OF OUR LARGE PUBLICLY-HELD CORPORATIONS HAS CAUSED A MONUMENTAL CHANGE FOR THE BETTER IN THE GOVERNANCE OF THOSE CORPORATIONS.

THE CHALLENGE OF THE MOMENT IS TO CONFRONT THE FACT THAT THE AMBIGUITIES INTERJECTED BY THE CRIMINAL SECTIONS OF THE FCPA HAVE PROVEN TO BE BURDENSOME AND NOW THREATEN THE EFFICACY OF THE SEC PROGRAM. A SIGNIFICANT REDUCTION OR ELIMINATION OF THOSE CRIMINAL PENALTIES WOULD ELIMINATE THAT BURDEN WITHOUT IMPAIRING IN THE SLIGHTEST THIS COUNTRY'S NOTABLE SUCCESS IN ELIMINATING THE KIND OF UNDESIRABLE CORPORATE CONDUCT THAT GAVE RISE TO THE FCPA.

TOO MUCH PRECAUTION CAN BE AS BAD AS TOO LITTLE. PERHAPS THE POINT HAS BEEN PUT BEST BY ROBERT FROST, WHO MANY YEARS AGO DEALT WITH THE FRUSTRATIONS OF ACCOUNTING, WHEN HE WROTE:

NOBODY WAS EVER MEANT
TO REMEMBER OR INVENT
WHAT HE DID WITH EVERY CENT.

Best Available Copy

1976 CORRESPONDENCE

BETWEEN

RODERICK M. HILLS
Chairman
Securities and Exchange Commission

AND

WILLIAM BATTEN
New York Stock Exchange, Inc.



SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

May 11, 1976

William Batten
New York Stock Exchange, Inc.
11 Wall Street
New York, N. Y. 10005

Dear Sir:

I want to take this opportunity to congratulate you again on your recent appointment and to wish you the best of luck. The job is a challenging one, but one I know you will fill with distinction. I speak for all the members of the Commission in saying that we look forward to working with you on the many complex problems facing the securities industry today. In that vein, I would like to advise you of a subject which Jim Needham and I have discussed informally in the past, and ask for the benefit of your thoughts.

As you know, the Commission has for many years advocated that publicly-held companies create audit committees, composed of independent directors, to work with outside auditors.*/ In our review of corporations who have revealed questionable foreign and domestic payments we have found an almost universal use of misleading financial records to conceal such corporate practices from outside auditors and directors and corporate counsel. The existence of an audit committee that meets privately with the outside auditors to discuss the scope of the audit, questions arising during the audit, including disputes with management, and that has access to the corporate financial information, is an important part of our effort to maintain the credibility of our system of corporate self regulation.

I am sure you are aware of the fact that the Auditing Standards Executive Committee of the A.I.C.P.A. has circulated an exposure draft of

*/ In 1940, following the McKesson-Robbins investigation, the Commission urged the formation of audit committees, composed of non-officer directors, to participate in arranging corporate audits. In 1972, the Commission endorsed the establishment of audit committees composed of outside directors for all publicly-held companies to provide more effective communications between independent accountants and outside directors, and thereby to safeguard further the integrity of corporate financial statements on which public investors rely. In 1974, in amending its rules to require disclosure in proxy statements of the existence or absence of audit committees, the Commission reiterated its support.

Best Available Copy

William Batten, Chairman
Page Two

a new auditing standard which, if adopted, would require auditors to bring any questionable payments that they may find to the attention of a level of management high enough for corrective steps to be taken. If questionable payments by top management are discovered, such an approach will, of course, be enhanced if an audit committee is in existence.

Additionally, there has been considerable recent comment about steps that can be taken to make the role of the board of directors more meaningful. Some major corporations have already taken steps to restructure their boards so that a majority consists of outside directors. Indeed, the Chairman of Connecticut General has recently written us about actions taken by that corporation to create a board consisting only of outside directors and the chief executive officer. While we have no firm notion about the optimum relationship between outside and inside directors, we do believe it is a subject of considerable importance.

Finally, many thoughtful commentators and many major law firms have come to the conclusion that the effectiveness of the board of directors and independent counsel is enhanced when the critical aspects of the two functions are kept separate. This, of course, raises the question of whether members of law firms which have the responsibility of advising the corporation, including the board, should also serve as members of that board of directors.

The importance of maintaining the truly independent character of the boards of directors of our larger corporations has been illustrated by the Commission's recent enforcement actions in the area of questionable or illegal corporate payments. Significantly, in some of these cases no audit committee existed. In the others, with a single exception, audit committees were either only operated during a portion of the time when the questionable payments were alleged to have been made, or not wholly independent of management. Accordingly, the resolution of these actions typically has involved the establishment of a committee comprised of independent members of the board of directors in order to conduct a full investigation, utilizing independent legal counsel and outside auditors to conduct the necessary detailed inquiries. The thoroughness and vigor with which these committees have conducted their investigations demonstrates the importance of establishing entirely independent audit committees as permanent, rather than extraordinary, corporate organs and encouraging the Board to rely on independent counsel.

William Batten, Chairman
Page Three

With these thoughts in mind, we have been considering various approaches to increase the likelihood that larger public corporations will establish audit committees composed of outside directors, that they will take further steps to make the role of the board of directors more meaningful, and that corporate boards will deal with independent counsel. One particularly promising approach to accomplish these goals would be for the Exchange to amend its policies and practices. As the Company Manual points out, the Exchange's listing agreement constitutes a code of performance to which companies commit when listing their securities on the Exchange. When the listing agreement was first instituted in 1899, the Exchange took the lead in the field of financial disclosure by requiring regular financial reports from listed companies; subsequently, independent public accountants were required.

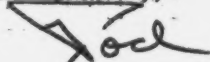
The Exchange's listing policies have expanded in scope over the years. Specifically, the Exchange has long urged the desirability of including outside directors on corporate boards and specifically charging them with ensuring full disclosure of corporate affairs. In its 1973 White Paper on financial reporting, the Exchange recommended that audit committees, preferably comprised exclusively of outside directors, be formed. This recommendation represented a reaffirmation of a principle first raised by the Exchange in 1940.

In keeping with this tradition, the Exchange now could take the lead in this area by appropriately revising its listing policies, thus providing a practical means of effecting these important objectives without increasing direct government regulation. The objectives are sound in principle and, if implemented, they would significantly advance the public interest.

We would very much appreciate receiving your views on whether the New York Stock Exchange would find it appropriate to alter its listing policies along the lines discussed above. We are sensitive to the fact that, to the extent the Exchange's listing policies impose burdens which corporations might otherwise avoid, the attractiveness of listing on the Exchange may be diminished. But, at the same time, the Exchange has frequently recognized that it could provide effective leadership where its initiatives were consistent with developments in public policy in the fields of corporation finance, management, stockholder relations and accounting, and recent surveys suggest that perhaps two-thirds of NYSE listed companies already have independent audit committees.

We look forward to receiving the benefit of your views, particularly as to what Commission action, if any, in this area would be useful. We would be pleased to meet with you to discuss these matters further.

Sincerely,



Roderick M. Hills
Chairman

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THE New York Stock
Exchange

William M. Eatten
 Chairman and
 Chief Executive Officer

Chairman Roderick M. Hills
 Securities Exchange Commission
 500 North Capitol Street, N.W.
 Washington, D.C. 20549

August 3, 1976

Dear Rod:

We have discussed your letter of May 11, 1976 and your various suggestions regarding boards of directors of publicly-held companies and particularly the creation of Audit Committees composed of Independent Directors of such companies.

Recently I furnished to you a report of a corporate policy survey conducted by the Exchange of 150 companies, 50 of which were selected from each of three groupings of 500 companies ranked in order by the number of shareholders of record. The top group (Cell A) contained the 500 companies with the largest number of shareholders of record, the middle group (Cell B) the 500 companies ranked 501 through 1,000, and the lowest group (Cell C) the 500 companies with the fewest shareholders of record. The results of the survey may be summarized as follows:

1. The top companies (Cell A) have more board members and a greater proportion of outside directors relative to the other sample company groups.
2. More than four out of five large companies (Cell A) consider a majority of outside directors the optimum proportion on their board as against only three of five among medium-sized (Cell B) and an even split among smaller companies (Cell C).
3. Very few companies, regardless of size, actually provide their board of directors or its committees with

New York Stock Exchange, Inc. 60 Broad Wall Street New York, New York 10005

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Chairman Hills
Page 2

August 3, 1976

the services of independent counsel.

4. Most companies oppose the idea of independent counsel or have no policy or opinion on the subject.
5. Seven out of ten top companies (Cell A) have an independent audit committee consisting of at least three outside directors, while only two of five small companies (Cell C), have one.
6. Almost one-quarter of the companies in the survey, made up mostly of medium and small-sized companies (Cells B and C) do not have any kind of audit committee.
7. More than four out of five large companies (Cell A) have their audit committee findings reported directly to the board, while only around half of the companies in the other two groups do.

The report on the survey contains its detailed findings which reflect varying views on the different issues raised in your letter of May 11, 1976. We have focused our attention on the subject of Audit Committees, and their composition. In that connection we have further analyzed the information received during the survey as shown on the enclosed schedules. Schedule A shows the detailed composition of 81 companies who have Audit Committees with three or more Outside Directors, Schedule B shows the composition of 35 companies who have Audit Committees that have less than three Outside Directors and Schedule C shows the size and composition of Board of Directors of 34 companies in the survey who do not have Audit Committees although a majority of these companies have at least two Outside Directors. Considering this information as representative of our listed companies I have attempted to fashion for your consideration and comment an Audit Committee which would better assure the integrity of a company's financial statement by utilizing on the Committee the knowledge and experience of Directors who although independent of judgment may not be considered an Outside Director by some definition. In wrestling with the problem of definitions I find it more difficult to define the term "Independent Director" than it is to describe the term "Outside Director". I believe

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Chairman Hills
Page 3

August 3, 1976

therefore that perhaps the term Outside Director describes but one class of Independent Director and not a limitation on its meaning. Attached you will find a draft of a proposal for Audit Committees which would:

1. Require the establishment of an audit committee consisting of a minimum of three Independent Directors.
2. Require that at least two of the directors of a three man audit committee be qualified as Outside Directors.
3. Permit but not require a Board of Directors to exercise its discretion in appointing a highly qualified former officer, who is a director of the company, to its audit committee.
4. Permit the Board of Directors to appoint an audit committee of more than three directors providing that a majority qualify as Outside Directors.
5. Based on our survey, permit listed companies to comply at a reasonably early effective date, after approval of the policy by self-regulatory and regulatory bodies. There would be no need to vary dates by which companies of various sizes must comply, but all companies would have sufficient lead time by which they must be in compliance.
6. Provide a measurable standard by which the policy could be administered by the Stock List Department.

After receiving your comments and making such modifications as may be appropriate, I would propose that we expose draft language to each of our listed companies for their views. Following that procedure and with the benefit of such comments as we receive, the matter would be submitted to our Board of Directors for their consideration and deliberation as to whether the policy should be adopted as an absolute listing and continued listing requirement. One of the considerations in that deliberation will necessarily be the potential enlarged liability of the Exchange with respect to the performance and functioning of Audit Committees of listed companies. I believe that the limit of that exposure must be reduced to a minimum.

I look forward to receiving your comments. In addition I also wish to confirm my invitation to you to speak to the Board of Directors at the luncheon which precedes our September 2 meeting. The luncheon is at 12:30, but I would be delighted to have you visit with me prior to that time.

Sincerely,



PROPOSAL FOR AUDIT COMMITTEES

Audit Committee of Independent Directors

Each company as a condition of listing and continued listing of its securities on the Exchange, shall provide in its by-laws or by appropriate resolution of its Board of Directors a requirement for the establishment of an Audit Committee consisting of a minimum of three Independent Directors, no one of whom shall be an officer or an employee of the company and at least two of whom shall qualify within the meaning of the term "Outside Director" as herein described.

The Audit Committee may in the discretion of the Board of Directors consist of more than three Independent Directors, but in no event shall the majority of such directors consist of other than "Outside Directors" within the meaning of the term.

Meaning of Terms

Independent Director - The term "Independent Director" shall include those who qualify as "Outside Directors" but may also include a former officer of the corporation who although receiving pension or other deferred compensation payments from the company is in the opinion of the Board of Directors a person who will exercise independent judgment and whose presence on the Audit Committee will materially aid and assist the function of the committee.

Outside Director - The term "Outside Director", with respect to an Audit Committee shall be persons who are not officers, or relatives thereof, employees, former officers, consultants, or persons who are not otherwise compensated on a regular basis by the company other than by directors' fees. The following are examples of persons who would not qualify as Outside Directors for purposes of an Audit Committee:

Outside Legal Counsel to the Company;

Anyone who would be or represent a controlling person under the SEC definition;

Anyone who would be an "associate" of an officer or controlling person under SEC definition.

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Schedule A

Detailed Composition of Independent Audit Committees with three or more outside directors

<u>Composition of Audit Committees with 3 or more Outside Directors</u>	<u>Total N=81</u>	<u>Cell A N=36</u>	<u>Cell B N=27</u>	<u>Cell C N=20</u>
<u>3 Man Committees</u>				
all outside directors	51	21	18	12
<u>4 Man Committees</u>				
all outside directors	10	4	2	4
3 outside and 1 inside	5	3	2	-
3 outside and 1 general counsel	2	-	-	2
<u>5 Man Committees</u>				
all outside directors	3	3	-	-
4 outside and 1 inside	3	-	2	1
3 outside and 2 inside	1	-	1	-
<u>6 Man Committees</u>				
all outside directors	4	2	2	-
5 outside and 1 inside	1	1	-	-
4 outside, 1 general counsel and 1 inside	1	-	-	1

Source: Corporate Policy Survey

Detailed Composition of Audit Committees
with less than Three Outside Directors

Schedule B

<u>Composition of Audit Committees with less than 3 Outside Directors</u>	<u>Total N=35</u>	<u>Cell A N=11</u>	<u>Cell B N=10</u>	<u>Cell C N=14</u>
<u>1 Man Committees</u>				
inside director	1	1	-	-
outside director	1	-	-	1
<u>2 Man Committees</u>				
both outside directors	7	-	3	4
<u>3 Man Committees</u>				
2 outside and 1 inside	12	6	3	3
2 outside and 1 general counsel	7	2	1	4
1 outside and 2 inside	1	1	-	-
1 outside, 1 general counsel and 1 inside	1	-	1	-
1 general counsel and 2 inside	1	-	-	1
3 outside (different definition)	1	-	1	-
<u>4 or More Man Committees</u>				
1 outside and 3 inside	2	1	-	1
2 outside and 1 inside	1	-	1	-

Source: Corporate Policy Survey

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THE New York Stock
Exchange

September 3, 1976

William M. Batten
Chairman and
Chief Executive Officer

To: Chief Executive Officers

All of us in the business community are well aware of the extent to which the broad issue of corporate accountability has been attracting public attention and government concern. Several months ago, Securities and Exchange Commission Chairman Roderick M. Hills suggested to me that the New York Stock Exchange might be uniquely positioned, through its close relationships with more than 1,500 of the nation's leading corporations, to help improve the climate of public confidence in U.S. business.

Accordingly, our Board is considering requiring every domestic listed company, as a condition of continued listing after December 31, 1977, to maintain an Audit Committee composed entirely of independent directors who are not part of current management.

We estimate that about 80% of all listed companies today have Audit Committees, although, in many cases, they include directors who are company officers or employees. A recent informal survey of representative listed companies leads us to believe that the vast majority agree with the Independent Audit Committee concept and would support Exchange initiatives to incorporate it into our listing requirements.

We also believe, however, that listed companies are entitled to a voice in major policy decisions affecting them and we are, therefore, seeking the views of the chief executive officer of every domestic company with common stock listed on the Exchange.

Attached you will find a draft proposal on which you are requested to comment so that our Board of Directors may have the benefit of your thinking for its deliberations at its regular meeting on October 7.

Under the proposal, the Audit Committee would consist of at least three independent directors, two of whom must be outside directors. No upper limit is placed on the size of the Committee, but in all cases, the majority of the Committee must be outside directors.

A simple reply form is enclosed for your convenience, and, of course, we will welcome any more detailed comments you or your associates may wish to offer. (Information copies of this letter are being sent to your company's Chief Financial Officer and Secretary.)

To facilitate tabulation of responses for presentation to our Board, it would be most helpful to receive your reply by Tuesday, September 21.

Sincerely,

Wm Batten

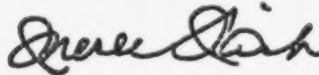
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THE New York Stock
Exchange

Merle S. Wick
Vice President

**TO: Corporate Secretaries of Listed
Companies**

Attached for your information is a copy of a letter and enclosures sent this date by Exchange Chairman William M. Batten to the Chief Executive Officer of every domestic company with common stock listed on the Exchange.



New York Stock Exchange, Inc. Division of Stock List 20 Broad Street New York, N. Y. 10005

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THE New York Stock
Exchange

PROPOSAL FOR AUDIT COMMITTEE

Audit Committee of Independent Directors

Each domestic company as a condition of listing and continued listing of its securities on the Exchange, shall provide in its by-laws or by appropriate resolution of its Board of Directors, a requirement for the establishment of an Audit Committee consisting of a minimum of three Independent Directors, no one of whom shall be an officer or an employee of the company and at least two of whom shall qualify within the meaning of the term "Outside Director" as herein described.

The Audit Committee may in the discretion of the Board of Directors consist of more than three Independent Directors, but in no event shall the majority of such directors consist of other than "Outside Directors" within the meaning of the term.

An Audit Committee meeting the above requirements shall be established no later than December 31, 1977.

Definition of Terms

Independent Director - The term "Independent Director" shall include those who qualify as "Outside Directors" but may also include a former officer of the corporation who although receiving pension or other deferred compensation payments from the company is in the opinion of the Board of Directors a person who will exercise independent judgment and whose presence on the Audit Committee will materially aid and assist the function of the Committee.

Outside Director - The term "Outside Director", with respect to an Audit Committee, shall be persons who are not officers, or relatives thereof, employees, former officers, consultants, or persons who are not otherwise compensated on a regular basis by the company other than by directors' fees. The following are examples of persons who would not qualify as Outside Directors for the purposes of an Audit Committee:

Anyone who would be classified as or represent a parent, controlling person or affiliate under SEC usage of these terms, or anyone who would be an "associate" of such person;

Anyone who would be classified as an associate of any officer or employee of the company;

Outside Legal Counsel to the Company.

**COMMENTS ON NEW YORK STOCK EXCHANGE
AUDIT COMMITTEE PROPOSALS**

Comments provided by: _____
 _____ NYSE Listed Company

Name of Respondent	Title
1. Do you agree that the Exchange should adopt a requirement regarding the Establishment of an Audit Committee?	
	Yes No
2. Do you agree that such committees should be composed of a minimum of three independent directors of which a majority must be outside directors?	
	Yes No
3. Do you agree with the deadline of December 31, 1977?	
	Yes No
4. Does your company already have an Audit Committee that meets the proposed requirements or do you have plans to appoint such a committee?	
	Yes No
5. If not,	
Will you, as Chief Executive Officer, implement the policy if it is adopted by the Exchange?	
	Yes No
or	
Will you recommend action by your Board if that is required?	
	Yes No
6. Other comments or suggestions:	

Your reply should be mailed to:

New York Stock Exchange, Inc.
 Stock List Division
 Audit Committee Study

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News Release

THE New York Stock
Exchange

11 Wall Street New York NY 10005 Phone (212) 6
TWX No 710 581-5464
Jack Brennan, Manager of Media Relations
Home Phone (212) 684-3083

September 2, 1976

Note to Editors:

The Board of Directors of the New York Stock Exchange voted today to circulate the attached proposal to chief executive officers of listed companies for their comments prior to formal consideration of the proposal at the board's regular meeting on October 7.

Att.

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PROPOSAL FOR AUDIT COMMITTEE

Audit Committee of Independent Directors

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Anyone who would be classified as or represent a parent, controlling person or affiliate under the SEC usage of these terms or, anyone who would be an "associate" of such person;

Anyone who would be classified as an associate of any officer or employee of the company;

Outside Legal Counsel to the Company.

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SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20540

September 10, 1976

William Batten
New York Stock Exchange, Inc.
11 Wall Street
New York, New York 10005

Dear Sir:

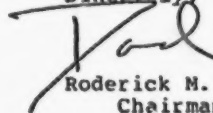
I was extremely pleased to receive a copy of your memorandum of September 3, 1976, to the Chief Executive Officers of domestic corporations listed on the Exchange, in which you solicit comment on a proposal to require listed companies to maintain an audit committee composed independent directors.

It is, at this juncture, not appropriate for the Commission to offer any observations on the substance of the particular requirement which your Exchange is presently considering. I would, however, like to express my great personal satisfaction with the Exchange's action in proposing a requirement relating to independent audit committees. As I stressed in my letter to you last May, the Commission has long advocated the creation of such audit committees for publicly held corporations, and believes that they are a critical instrument for enhancing the integrity of corporate accountability upon which this nation's free enterprise system is predicated. Accordingly, I am gratified that, under your leadership, the New York Stock Exchange has initiated affirmative steps in this important area.

In a broader perspective, I also believe that the type of action you have proposed could prove to be an excellent example of the efficacy of the concept of industry self-regulation which underlies the Securities Exchange Act. To the extent that the self-regulatory bodies take the initiative to assure that those persons and entities subject to their jurisdiction conform to the high ethical standards which the public expects of American business, the need for direct government regulation of business is correspondingly reduced. In the context of the Commission's responsibilities, this is, I believe, the essence of the type of regulatory reform which this nation's leaders are advocating.

The Board of Governors of the Exchange have our great respect for this first step on the issue of independent audit committees. I am confident that your efforts will provide a significant impetus for a better public view of the American business community.

Sincerely,


Roderick M. Hills
Chairman

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Schedule C

Size and Composition of Boards of Directors of Listed Companies without Audit Committees

Board Size and Composition	Total N=34	Cell A N=5	Cell B N=13	Cell C N=16
<u>5 Man Board</u>	<u>2</u>			
all outside		1	-	-
1 outside, 4 inside (1 counsel)		-	-	1
<u>6 Man Board</u>	<u>4</u>			
2 outside, 4 inside		1	-	1
2 outside, 3 inside, 1 counsel		-	-	1
1 outside, 5 inside (1 re- hired officer)		-	1	-
<u>7 Man Board</u>	<u>3</u>			
4 outside, 3 inside		-	1	1
3 outside, 4 inside (1 relative*)		-	-	1
<u>8 Man Board</u>	<u>5</u>			
4 outside, 4 inside		1	-	1
2 outside, 6 inside		-	1	-
2 outside, 5 inside, 1 counsel		-	-	1
1 outside, 6 inside, 1 counsel		-	-	1

<u>Board Size and Composition</u>	<u>Total N=34</u>	<u>Cell A N=5</u>	<u>Cell B N=13</u>	<u>Cell C N=16</u>
<u>9 Man Board</u>	<u>4</u>			
5 outside, 3 inside, 1 counsel		1	-	-
4 outside, 5 inside		-	1	-
3 outside, 6 inside		-	-	1
1 outside, 8 inside (1 retired officer)		-	-	1
<u>10 Man Board</u>	<u>7</u>			
6 outside, 4 inside		-	-	1
4 outside, 6 inside		-	1	-
4 outside, 5 inside (2 retired officers), 1 counsel		-	1	-
3 outside, 7 inside (1 retired officer)		-	1	-
2 outside, 7 inside (4 relatives*), 1 counsel		-	1	-
2 outside, 8 inside (1 relative*)		-	1	-
1 outside, 9 inside		-	-	1
<u>11 Man Board</u>	<u>1</u>			
7 outside, 3 inside, 1 counsel		1	-	-

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<u>Board Size and Composition</u>	<u>Total</u> <u>N=36</u>	<u>Cell A</u> <u>N=5</u>	<u>Cell B</u> <u>N=13</u>	<u>Cell C</u> <u>N=16</u>
<u>12 Man Board</u>	<u>4</u>			
3 outside, 4 inside		-	1	-
2 outside, 6 inside		-	1	-
1 outside, 11 inside (4 retired employees)		-	-	1
1 outside, 11 inside (5 relatives*)		-	-	1
<u>13 Man Board</u>	<u>1</u>			
6 outside, 7 inside		-	-	1
<u>15 Man Board</u>	<u>3</u>			
4 outside, 11 inside		-	-	1
3 outside, 12 inside (1 officer)		-	1	-
3 outside, 10 inside (1 officer), 2 counsel		-	1	-

* Refers to relatives of company founders, officers, employees, retired officers or retired employees.

Note: Items in parentheses are included in the count already given for inside directors.

Mr. WIRTH. Thank you very much, Mr. Hills. I would hope, again as I have pointed out, that after we have gone through the panel, we might be able to go back and get each of you to comment on what the others have said.

Some of you might wish to do that as we go along.

Dr. Clinard.

STATEMENT OF MARSHALL B. CLINARD

Mr. CLINARD. Before going to the University of New Mexico, I had retired recently at the University of Wisconsin. During my last 2 years there I had a grant from the Department of Justice to study the illegal behavior of corporations. I published a good deal since then, through the U.S. Government Printing Office and other publications. In my study of the illegal behavior of the Fortune 500, I went into the problem of corporate bribery abroad. I studied at least 30 very large documents dealing with disclosures of corporations to the SEC which I obtained under the Freedom of Information Act as well as a large amount of other material from various other sources.

In speaking here I will be a bit negative perhaps about corporations, but my interest is in trying to protect American corporations.

I think we have to realize that historically the large corporations in America have been under long-term public suspicion. Grover Cleveland, Theodore Roosevelt, Woodrow Wilson, Franklin Delano Roosevelt, and others, passed extensive legislation to regulate them.

I might say that contemporary polls show great suspicion of the behavior of corporations. Nothing, however, tarnished more the reputation of corporations, I think, than Watergate and particularly the foreign bribery cases.

I think to change present law, which I feel is quite effective, will lay open very, very severe attacks upon corporations.

As it is now, nearly all corporations, according to the Wall Street Journal articles I read, now have codes of ethics stated in black and white forbidding foreign bribery.

To weaken the present would be, in the light of world opinion, I think, extremely dangerous.

We would have to go on record in countries throughout the world that we have decided to do something contrary to what is now in corporate codes of ethics.

Another point I would like to make is that if Japan bribes, if Belgium bribes, if France bribes, if England bribes, I don't think that attracts much world attention, but when the United States, one of the two great superpowers, does it, that does attract world comment and does, in my judgment, endanger the position of the United States in the world.

I have made a study of the methods of payments that were made on these bribes. I am not talking about the size of them, how they were done through foreign subsidiaries, dummy corporations, sales agents, et cetera. In my written testimony I spelled out about 20 very detailed methods.

I have never seen such elaborate and so cunning an effort to conceal within corporate accounting the bribery that they had been doing.

This indicated to me either that the corporation knew that it was potentially illegal and unethical, but they also felt that in the light of public opinion it was very highly embarrassing to the public image of the corporation if it became known. I have outlined in my written testimony the different types of concealment practices. I think one can say that the use of bribery of foreign officials might increase our exports somewhat. The evidence has not been too great that it would; I don't think the economic effect has been that serious.

We have to weigh the basic question, What is the price that we as Americans are willing to pay for endangering the political position of the United States and the stability of the nations involved?

I shall try to summarize, what foreign bribery does.

It seems to me that it represents an inconsistent attitude between foreign and domestic activity. Corporate bribery is widely prohibited in this country whether political or commercial bribery. To put it another way, how would we, as Americans, react if foreign corporations bribed our Government officials and members of Congress as Tongsun Park of Korea tried to do several years ago to some of our own Congressmen?

What would happen if the Japanese, in order to get more car sales over here, would bribe our high Government officials?

Two, I think the studies show overseas bribes may negatively affect foreign governments and tarnish the image of the United States abroad. Although a corporation may well gain some immediate profit through such payments, the bribery of foreign officials may seriously endanger our relations with other countries and the American image among the general population of the country, particularly since we are a superpower.

In my judgment there is ample evidence, for example, from the statements of the Iranians, that our hostages were held, in part, because of the bitter antipathy the Iranians have toward us, partly because American corporations paid bribes to many officials including a \$3 million bribe to the commander of the Iranian Air Force. It is well known that these bribes were kicked back to the Shah, and became part of his personal fortune.

Foreign payments, moreover, are generally concealed from the host country. The moneys employed in the transaction, particularly through payments to corporation agents, often violate the foreign currency or tax laws, when, for example, they are paid through Switzerland.

Three, foreign bribery negatively affects the developing countries. I think this is extremely important. The United States over the years has contributed billions of taxpayers' dollars to improve the economic condition and the political stability of the developing countries. In fact, it has contributed far more financial support for these countries probably than all the other countries in the world put together.

It has been partly for humanitarian reasons, but partly to counteract the countries that might fall in the Soviet orbit. To me it makes little sense, therefore, for U.S. transnational corporations,

after we have spent all its money, to endanger those goals through bribes that increase their own financial gains but at the same time corrupt officials and lead to the destabilization of those countries by military coups or by Marxist infiltration.

Four, foreign bribery can be injurious to the corporation itself. Studies indicate that it may well endanger the effective internal operations of the corporation, abetting the corruption of public officials of the foreign countries. A corporation may help to corrupt itself as well as the institutional integrity of that corporation at home. The attitudes of its own employees may well be affected.

Five, the credibility of foreign financial statements are endangered by foreign bribery. That has already been commented on, but I might point out that the term "material" being interjected into accounting rules seriously endangers the credibility of the records that would be kept.

Six, foreign bribery produces unfair competition between those U.S. corporations that do bribe and those that do not. In my testimony I have indicated a considerable number of corporations that did not engage in foreign bribery. It is also quite important to realize that U.S. corporations compete against each other to bribe foreign officials to secure sales. It is not limited to competition with foreign corporations.

It is my understanding that such bribes are a violation of the antitrust law. Competing U.S. corporate bribes moreover, if successful, do not add to the U.S. balance of payments, when the sale would probably have gone to the U.S. corporation anyway.

It is illogical to exempt foreign bribery where "customary", in a country. This position is both illogical and dangerous. Such an exception would seriously endanger the entire system of control over corporate bribery.

To follow this position to its logical conclusion, a host of corporate business practices in this country would be exempt from the law, because they are "customary" ways of doing business. Political contributions, commercial kick-backs, false and misleading advertising, polluting the environment are all often regarded as "customary" business practices.

Furthermore, who is to say what is customary in a given country? One American corporation may make a judgment that bribery is customary, and another may say that is not. Certainly I can say from having worked in developing countries a great deal that not all public officials in any country by any means can be subject to bribery.

Furthermore, the legal codes of virtually every nation in the world prohibit the acceptance of bribes by their officials.

In conclusion, then, the Foreign Corrupt Practices Act appears to have corrected a serious problem; likewise, it seems to have operated quite successfully. Our nonagricultural exports have not materially suffered, and in cases where they have been affected it has, in all likelihood, been due primarily to other causes. Virtually to scuttle the present law, as certain clauses in the proposed amendment actually do, with the hope of obtaining additional financial returns by certain corporations, is not in accordance with my conception of the proper role of the United States in the turbulent political world of today.

[Testimony resumes on p. 73.]

[Mr. Clinard's prepared statement follows:]

STATEMENT OF
Marshall B. Clinard

Multinational U. S. corporations have contributed enormously to the industrial and commercial development of the United States and to the Western world, as well as increasingly to the developing nations. Simultaneously with the rise of the great productive power of these giant corporations there has evolved an equally great potential for significant social harm, a potential that has far too often, unfortunately, become a social reality.

The social harm that multinational corporations can create has been demonstrated in a number of ways. They have on occasion, and for their own ends, exercised undue political influence on the United States government and on foreign governments as well. The ethics and the social responsibility of many transnational corporations has been severely questioned. Evidence of law violation is extensive. To mention only a few types, violations have resulted in large economic losses to consumers and to competitors through price fixing, for example, to the injury or death to thousands of persons, including employees, as the result of unsafe drugs and other various consumer products, as well as in unsafe working conditions and the pollution of the environment. It is within this larger perspective, then, that the problem of payoffs to foreign government officials must be examined, not as an isolated issue.

The size of large U. S. corporations staggers the imagination. The total sales of the Fortune 500 largest industrial corporations in 1979 was 1.2 trillion dollars. These sales account for two-thirds of all industrial sales, and more than three-fourths of all manufacturing assets. In 1980 the sales of the 10 largest U. S. corporations ranged from 25 billion to 103 billion. In 1980 Exxon, the largest industrial corporation, had sales of 103 billion, Mobil as second had 59 billion, and General

Motors, at third had sales of \$58 billion. Few of the world's other corporations can compare in size with the largest U. S. corporations. Sales of the top 10 foreign corporation⁷ in 1979, ranged from \$16 billion to \$59 billion for Royal Dutch Shell; none of the largest are Japanese.

Various surveys have shown that it has been substantially easier for many large U. S. corporations to make profits in their overseas operations than in this country. As a result, large U. S. corporations have been shifting more and more of their assets and sales abroad; foreign assets for many industries vary from 40 to 75 percent. Consequently, multinational corporations have the power to trade across national boundaries almost as if they do not exist. Exxon, for example, operates in more than 100 countries. The composition and complexity of these giant multinational corporations may result in a dual loyalty, one in which the corporation may experience difficulties in perceiving that what may be beneficial to them in their dealings abroad may actually be resulting in injury to the political and the national interests of the United States, as exemplified in the case of bribery of foreign government officials. In one sense, these industrial giants have become private governments.

U. S. corporate giants wield immense economic and political power both on the national and the international scene. Their enormous size and economic and political power dwarfs many nation-states, particularly in respect to most African, Asian, and Latin American countries. These transnationals may attempt to manipulate the economic goals and political processes or the very stability of a country. Sometimes through evasion of the law and sometimes through outright violation of the law, transnational corporations manage to play one country's laws off against those of another. A multinational may, for example, shift its operation to a subsidiary in one country

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to another, one in which the pollution or worker safety laws are more lax. Through transfer pricing corporations can bypass exchange regulations by means of inflated prices for imports, avoid their tax liability through artificially increased overseas prices, and evade custom duties by underpricing.

Why are Some Corporations Law Abiding and Others are Not?

A substantial proportion of large corporations appear not to violate the law. In a study I conducted, for example, approximately 40 percent of a sample of 477 Fortune 500 firms were not charged with any violation of a law, either minor or serious, by 25 federal agencies during a recent two-year period. Although a large percentage of the giant corporations engaged in substantial foreign payoffs, still many of them had little or no involvement, firms like IBM, Bendix, Pitney-Bowes, and Atlantic Richfield. In general, illegal behavior is more likely to be concentrated in certain industries and in certain corporations. In my research, for example, 38 of the 300 largest manufacturing concerns cited for violations, or 13 percent, accounted for 52 percent of all violations, an average of 23.5 per firm; serious violations showed similar disproportions. Many laws exist to protect law-abiding and ethical corporations that have demonstrated a sense of social responsibility from firms with different values.

It appears that a basic reason for some corporations to engage in more unethical and illegal behavior lies within the normative patterns within the corporation, with top management frequently setting the ethical tone for the lower management and personnel levels. In fact, a corporation can socialize its members to normative systems conducive to criminality. As Sporkin, former head of the enforcement

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division of the SEC, has said: "Some of our largest corporations have trained some of our brightest young people to be dishonest." Some corporations have set the pattern for others to follow. Lockheed, for example, appears to have set the pace on foreign pay-offs in Japan; Lockheed's chairman testified before a Senate sub-committee hearing, "If you are going to win it is necessary." Yet the officials of Northrop Corporation, which made payments as did Lockheed and through a special Swiss subsidiary to handle them, testified that they had learned how to do it from Lockheed.

The gigantic size of transnational corporations requires that corporations delegate decision-making and disperse operating procedures. Size, delegation, and responsibility combine to produce an organizational climate in some corporations that permits the abdication of a degree of personal responsibility for decisions that may allow individuals to remain personally almost entirely unaccountable for these decisions. At the highest levels executives can absolve themselves of responsibility, whether it be for foreign bribery or other law violations, through the rationalization that illegal means of attaining their stated goals of sales maximization had been devised and carried out without their knowledge. To the extent that middle and even lower level managers in some corporations feel that unethical and illegal behavior is needed to accomplish corporate goals, indeed that they may be indirectly coerced into it, the basic sense of personal moral responsibility may also be blunted. A successful conspiracy to violate the law, as in the case of foreign bribes, lies in the fact that some top executives do not ask what is going on and the lower levels wisely do not tell them.

Negative Attitudes of the Public to Large Corporations

The American public has long been concerned about the excessive power and the improper conduct of large U. S. corporations. In the early 1880s the public was concerned that Big Business was exploiting the nation's resources. Labor became concerned about this power, as did small businessmen. As a result of these concerns, the Sherman Anti-Trust Act was passed in 1890. This Act was directed at trusts and corporate monopolies. A dozen years later Theodore Roosevelt led another crusade against large corporations, as did Woodrow Wilson, all of which led to increased legislation. As an aftermath of the Great Depression, Franklin Roosevelt put through many strict controls on the corporations, and these controls were widely supported by the public. In recent years surveys have found widely held opinions that corporations are primarily motivated by self-interest rather than the national interest, that concern for the well-being of individuals is minimal, that profits are excessively high, and that the quality of products is frequently not reliable.

In spite of the long-term public suspicion of, and the general negative attitude toward, corporations, nothing has so tarnished their image within recent years as the public revelation of the widespread illegal corporate political contributions, domestic bribery, and the large foreign payoffs that were revealed in the 1970s. The SEC found that by 1978 illegal and/or questionable domestic and foreign payments totaling over \$1 billion had been made by 300 of the Fortune 500 leading industrial corporations.

Illegal Corporate Political Contributions

In order to understand the general setting in which corporate payoffs to foreign officials are made, one should keep in mind that illegal corporate contributions and pay-offs have long been part of the domestic political and commercial scene in this country. So bad was domestic corporate political corruption that since 1972 corporations have been prohibited from making direct contributions to candidates seeking election to federal office; many states have had laws against them for a much longer period of time. Like foreign bribery, such political contributions have generally had an economic purpose, that is to secure bureaucratic favors and to influence legislative and bureaucratic decisions that affect corporate profits. During the Watergate investigations it was revealed that more than 300 major corporations had illegally contributed large sums of money to the Nixon campaign. Most of these payments involved extensive deception, including false bookkeeping entries, mislabeling of accounts, and the maintenance of phony subsidiaries. As in the case of foreign bribery, some of the corporations involved defended their contributions as having been "extorted" from them, although the contributions were given in the active self-interest of the corporation.

Domestic Commercial Bribery

Even more similar to foreign payoffs is the domestic bribery that has a long history in a wide variety of business areas. These bribes or kickbacks to employees of other concerns take the form of illegal rebates, of commissions for alleged services, of money and gratuities of many types, including loans. What previously was a case

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subject to a private business suit has increasingly become a matter of government intervention. Under IRS codes, with few exceptions, tax deductions are not allowable for commercial bribery; kickbacks also violate other laws, such as laws that regulate alcoholic beverage controls and maritime shipping regulations. Such payments are, on the whole, concealed on the company books and constitute unfair competition as defined by the FTC, restraint of trade by the Sherman Antitrust Act, and, if they are not disclosed, violations of SEC regulations.

Foreign Payoffs or Bribery

Corporate payments to officials of foreign governments thus represent simply another form of illegal payments that, if they should largely be condoned as ⁱⁿ the revised version of the Foreign Corrupt Practices Act proposes, would actually mean the condemnation of these practices at home but not abroad. U. S. corporations would thus be operating under two different standards. Foreign corporate bribes are given for several reasons: to secure business, to retain business, to avoid harrassment, to reduce taxes, to induce official action, and to reduce political risks. The extent of such payments, as well as their size, have shocked the American people: as of 1976, 32 corporations alone in the Fortune 500 had reported such payments of more than \$1 million. Lockheed had made secret payments totaling at least \$25 million to foreign government officials, and they had paid in excess of \$200 million to various consultants, commission agents, and others. ITT had made payments of \$8.7 million to numerous countries, including Iran, Indonesia, the Philippines, Algeria, Mexico, Turkey, Chile, and Italy. Hospital Corporation of America was charged by the SEC with having made payments of \$4.3 million

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to persons of influence and power in Saudi Arabia. Some foreign bribery payments were extremely large. Lockheed, for example, paid \$12.6 million in bribes to Japanese officials, including ⁵1.6 million to Japan's prime minister. More than \$1 million was given to Prince Bernhard of the Netherlands for his influence in securing a contract. Textron's Bell Helicopter made payments of \$3 million to a high Iranian official between 1973-1975, as well as payments ranging up to \$400,000 to government officials in nine other countries, including Ghana. McDonnell Douglas was indicted for defrauding Pakistan International Airlines by concealing ^{from PIA} more than \$1 million in payments made to four of Lockheed's Pakistani agents. Lockheed was also indicted for paying \$400,000 to the chairman and vice-president of Philippines Airlines, \$2.1 million to three Venezuelans in connection with aircraft sales to the government-owned airline, and \$625,000 to Zaire's minister of transportation as well as to the governor of the National Bank of Zaire. Such examples are only a few of many: all of the payments were carefully concealed from the United States and the foreign governments, from the corporation stockholders, and from the public until they were forced to reveal them.

Many of the decisions regarding the foreign bribes are made at the highest corporate levels; in other cases, the internal organization of the transnational corporations seems to facilitate the use of bribery at lower levels. Often top executives delegate responsibilities, but their failure to follow up on them creates a general atmosphere in which corruption can exist and even flourish. In such a milieu the executives may issue directives exhorting employees to obey the law, yet at the same time they may fail to follow up on the general firm compliance level. They may not

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watch closely the day-to-day activities of subordinates, following simply various output measures like sales, market shares, or profit margins to evaluate foreign operations, all of which tends to put pressures on lower management levels to use bribes. Although management as well as stockholders may genuinely wish to prevent an environment in which employees or their agents accept bribes for price discounts, they may prefer to be blind to cases in which their sales personnel pay bribes to obtain lucrative deals." It is for these reasons that it is essential that the clause in the original bill "having reason to know" be retained with reference to corporate executives.

Methods of Payment. In nearly all of a large number of the cases that I have examined, corporate efforts to conceal their foreign payments were so elaborate and so cunning that even a casual examination would clearly reveal that the corporation involved had considered such behavior to be potentially illegal and unethical, at the least highly embarrassing to the corporate image.

Although direct corporate payments to foreign officials are simpler, greater are the risks of their being discovered. Thus indirect clandestine payments through other intermediaries have been common; they have involved foreign subsidiaries, dummy corporations, and sales agents. Payments are made through foreign subsidiaries with little control by the parent corporation, making it most difficult to trace the payment origin; or a subsidiary may be used to handle the foreign payoff by the parent corporation. Often used are dummy corporations, which are set up by the parent firm with no purpose other than to serve as a funnel for illegal transactions. Sales commissions are paid by the parent firm to the dummy corporation, and the payment is then passed on to independent agents for distribution as payoffs. The corporation can

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thus claim no knowledge as to whom payments have been made and, therefore, the payments cannot be linked to it. A dummy corporation was set up by Northrop Corporation in Switzerland for the purpose of paying some \$30 million in questionable and illegal commissions and to bribe government officials and agents in the Netherlands, Iran, France, the Federal German Republic, Saudi Arabia, Brazil, Malaysia, and Taiwan. Through this method payoffs were made to influential persons in these countries who had helped Northrop sell airplanes.

The most commonly used method of channeling foreign payments, however, is through a "sales agent" of the corporation who is located in a particular country. Through their knowledge of the channels and through the use of corporate bribes these agents can facilitate marketing arrangements. In a sense, they are retained by the corporation "to do the firms' dirty work," as they are not directly hired by the corporations as regular employees. An agent is generally paid a fee on a percentage basis of the total contract, and from this payment he then pays the third parties. With the recognition of the important role of agents in foreign payments, it is important to retain the wording in the original bill which forbade corporate payments to an agent while "knowing or having reason to know that it will be passed along to a foreign official."

Concealment Practices. For the purpose of conveying a bribe to a foreign recipient, for the protection both of the transnational corporation and the recipient from action by the latter's government, a number of secretive means have been devised. These "camouflaged" means, which are used far more frequently than straight cash payments, include overbilling of sales with kickbacks to buyers, gifts of property (watches,

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jewelry, payment of travel and entertainment expenses, provision of unsecured loans that are then not collected, placing relatives on payrolls as "consultants," providing scholarships and educational expenses for children, and deposits in numbered foreign bank accounts. Politicians who are "on the take" usually prefer payments through deposits made to numbered Swiss bank accounts, although Japanese politicians generally preferred direct payments, and in yen. United Brands deposited \$1.25 million to a numbered Swiss bank account in making payoffs to Oswaldo Lopez Arellano, former Honduran President-General. In the case of the well-known \$1.1 million "commission" paid to Prince Bernhard, payment was channeled through a Swiss lawyer and deposited in installments during 1960 and 1962 in a Swiss bank account in the name of the husband of the Prince's late mother, the number being supplied by him to the Lockheed representative. Originally Prince Bernhard had solicited a \$4 million payment from Lockheed in order to facilitate a contract from the Dutch government.

I made a detailed examination of disclosures to the SEC from 24 corporations involved in foreign payments. These disclosures indicate the wide range of practices used to conceal the payments. They included the following:

1. Distribution of misleading and false annual reports to both stockholders and to the SEC.
2. Payments from a bank account maintained in the name of certain employees of the corporation and used for bribes; improper payments made through an off-balance sheet bank account maintained in the name of an officer of the company.

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3. Illegal payments made to employees for so-called extra work and then diverted for bribes. In other cases there is "overpayment" of salaries and expenses to subsidiary employees.
4. Payments made by a foreign subsidiary described on the corporation's books as "community services."
5. Payments not recorded on the books at all.
6. Payments from reimbursements to the subsidiary by the corporation for certain expenses incurred in foreign operations but not actually involving the subsidiary.
7. Payments from the proceeds of a non-interest bearing, demand loan made to the subsidiary by its president or vice-president, which indebtedness was not recorded on the subsidiary's books.
8. Payments made to third parties who gave the money to those bribed.
9. Payments transferred to secret foreign bank accounts, particularly Swiss. In a special report to the SEC, Lockheed admitted "the accumulation in bank accounts and safe-deposit boxes in Switzerland of approximately \$751,000 and the payment from this amount of approximately \$292,000 to third parties.
10. Off-book funds derived from insurance premium refunds payable to foreign subsidiaries and maintained in the names of subsidiary officers.
11. False overbillings of sales to foreign customers so that the kickback became the bribe.
12. Delivery of payments in cash to avoid detection.
13. Utilization of so-called shell corporations either to enter into consultant agreements that served as a screen for questionable payments or to provide false receipts for payments actually made to third parties such as customers' employees.

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Arguments against Foreign Payments and in Support of Present Law

It is difficult to find any real rationale for a change in the present Foreign Corrupt Practices Act other than putting corporate profits before principles. The bill had the overwhelming support of the public and of Congress; the original bill, for example, was passed 86-0 by the Senate. The accounting sections of the bill were drafted by leading accountants in conformity with existing accounting practices and in line with the legal requirements of the SEC. A great difference exists between the requirement of records "in reasonable detail" and the recording only of transactions that have "material" impact. "Material" transactions, obviously, would be subjective and would, presumably, only mean that larger bribes would be included in financial statements.

During the four years that the act has been in operation only two cases of illegal payments to foreign officials have been brought by the SEC; three have been filed by the Justice Department. The SEC, however, has filed about half a dozen cases under the law's accounting section that requires corporations to have internal accounting controls that give a reasonable assurance that the financial records are accurate. It is possible, of course, that illegal practices are being more cleverly concealed, although this is hard to imagine with Stanley Sporkin as SEC enforcement chief during most of this period. Our non-agricultural exports have doubled during these years; although there has been a decline in the U. S. percentage of foreign trade it has been slight and may more logically be attributed to the increase in the value of the dollar and other factors.

This is not to say that the wide use of bribery of foreign officials might not bring about some increase in our exports; if so, the basic question is what price are we willing to pay for endangering the political position of the United States and the stability of other nations,

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particularly those in the process of development. Other important questions at stake are the effects of foreign bribery on the general climate of corporations and of pitting one U. S. corporation against another. More specifically, some of the arguments against foreign payments and in support of the present law are the following:

1. Foreign bribery represents an inconsistent attitude between foreign and domestic business activity. To permit foreign bribes but not to permit them at home presents an inconsistent ethical climate. Political and commercial bribery are largely prohibited in this country. A case before the federal courts in 1981 involved General Electric bribery in Puerto Rico. Although Puerto Rico is a commonwealth the people of Puerto Rico are U. S. citizens. In this case, which demonstrates how thin is the line between domestic and foreign bribery, a bribe of \$1 million had been given in 1973 to a Puerto Rican official of the Puerto Rican Water Resources Authority by General Electric to win a \$93 million power project contract over Westinghouse and other competitors. The indictment charged that the official had provided confidential information that gave G. E. a competitive edge over other U. S. corporations and that G. E. had furnished the bribe money through a Bermuda company. General Electric was convicted and fined, and two high G. E. executives were given prison sentences.

To put the shoe on the other foot, how would we react if foreign corporations bribed our government officials and members of Congress? Public reaction was strong, for example, when Tsongsun Park, a Korean entrepreneur, was charged in 1976 with being overly generous with dozens of Congressmen in order to win approval of issues beneficial to him and to the Korean government.

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2. Overseas bribes may negatively affect foreign governments and tarnish the image of the U. S. abroad. Although a corporation may well gain some immediate profit through such payments, the bribery of foreign officials may severely endanger our relations with other governments and the American image among the general population of the country. Being a super-power, the U. S. is not in the same position as are European countries or Japan; foreign bribes by British, West German, or Japanese corporations do not have the same effect on that country's image or position in the world. Yet it would be a mistake not to think that many other exporting countries are not also concerned with foreign bribery by their corporations. Foreign corporations have not always avoided difficulties by their foreign bribes, even when legal. A leading Belgian concern, for example, not only damaged its reputation but went into bankruptcy in 1979 because of the \$282 million in secret commissions it had paid out to secure a \$1.2 billion hospital project in Saudi Arabia. A brother of the Saudi King played a leading role in the mission negotiating the contract. The Belgian foreign minister, moreover, delivered an attack on the concern and private business in general, asserting that such lack of rigor, caution, and sense of responsibility had endangered the reputation of Belgian industry abroad and even the prestige of the state itself.

Foreign bribery by U. S. corporations certainly gives ample ammunition to political extremists in most countries. Large-scale U. S. corporate bribery in Iran, for example, contributed substantially to the 1979-1980 extreme anti-American sentiment in Iran, the taking of the U. S. embassy hostages, and anti-American sentiment today. Bribes to high-ranking Iranian officials by U. S. corporations contributed to the overthrow of the Shah by fueling growing political dissent regarding the

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Shah's oppression and U. S. complicity in this extensive corruption. These large-scale bribes in Iran by several large American corporations to the Shah's generals and other high officials, largely through sales agents, became well known, particularly because kickbacks were often given to the Shah personally. During a four-year period Textron's Bell Helicopter division, as well as at least six other suppliers, furnished large "fees" to Air Taxi Company, the Teheran sales agency owned, in part, by General Khatami, Commander of the Iranian Air Force. Rockwell International deposited \$547,602 to Air Taxi's account, from which a substantial check was drawn for General Khatami. More specifically, according to the SEC, Textron furnished \$3 million in questionable payments to Iranian government officials between 1973-1975. Grumman Corporation paid \$2.9 million through two agents described as a "bagman" and an "errand boy" for various military higher-ups in Iran. Lockheed's bribe of \$1.2 million to Prince Bernhard almost brought down the Royal House of the Netherlands. Japan's prime minister was dismissed from office and indicted for having received a \$1.6 million bribe from Lockheed, which had been paid, incidentally, through extremely devious methods. Whether the large American payoffs in Saudi Arabia will contribute to the destabilization of that country is yet to be seen.

Foreign corporate payoffs, moreover, are also generally concealed from the host country. The means employed in the transactions frequently violate the country's foreign currency or tax laws. Frequently, the methods of paying foreign sales commissions facilitate the avoidance by sales agents of local taxes or violate the exchange control regulations. Payments may be made, for example, through deposits in Swiss bank accounts. It was reported, for example, to the SEC by Uniroyal that specific prac-

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tices were used to conceal illegal payments from the foreign country. A memorandum from a company official abroad, in asking that the foreign payments be concealed, stated: "People in these countries risk prison and confiscation of their businesses if the government finds out that they keep commissions abroad."

3. Foreign bribery negatively affects the developing countries.

The United States over the years has contributed billions of taxpayers' dollars to improve the economic condition and the political stability of the developing countries. In fact, it has contributed the major part of foreign financial support for these countries. This financial assistance has been given partly for humanitarian reasons but likewise to maintain the political and military security of the United States on the world scene by preventing them from falling within the Soviet orbit. It makes little sense, therefore, for U. S. transnational corporations to endanger these goals through bribes that increase their own financial gains if, at the same time, their actions corrupt high foreign government officials and leads to the destabilization of the countries.

Bribes to foreign officials, moreover, do not contribute directly to the economic development of the host country; rather, they enrich individuals who, in turn, may deposit the funds abroad, in violation of the currency laws of their own countries. Such bribery, benefiting individuals as they do, fail to benefit the countries. In addition, the corruption of high officials in developing countries is likely seriously to affect lower echelon public service personnel and students in both secondary schools and universities. Above all, corruption in high places undermines the average citizen's faith in his own country's institutions and in its politicians. Consequently, this loss of

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faith and respect can facilitate military coups and Marxist revolutions. The fact that the corporate bribe may have been solicited by the government official does not help to minimize the overall affect on the long-term political stability of the country.

4. Foreign bribery may be injurious to the Corporation itself.

It may well endanger the effective internal operations of the corporation. In abetting the corruption of public officials of other countries, a corporation may help to corrupt itself, as well as its institutional integrity at home. The attitudes of its own employees may well be affected. Some corporate executives, in fact, have fully recognized that corruption abroad may be deleterious at home. The chairman of the board and president of Pitney-Bowes, a billion dollar corporation, took a firm position on this issue, with the result that foreign payments made by his firm were miniscule. In a statement to company stockholders, Fred Allen said: "I have spoken several times on the general subject of corporate morality-- particularly with regard to the bribery of foreign officials, but also concerning all types of wrongdoing and whether in the United States or any other country. When we consider corporate morality . . . no price is too high." Michael Blumenthal, then chief executive officer of Bendix Corporation and later Secretary of the Treasury, stated: "I insisted that the company pay not one penny in bribes. I was told that we could not do that -- that we would lose business. Well, we didn't. What did happen was that we attracted the best graduates of Harvard and Stanford, who had read about us. It helped morale at Bendix." Unfortunately, non-bribing corporations did not generally speak out against such behavior by others. Some later had regrets. A high official of Eli Lilly and Company later stated: "We blew our chance. When there were some 100 companies bribing,

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including several drug companies, we weren't. We should have spoken out against the practice and distinguished ourselves. But we didn't."

5. The credibility of corporate financial statements are endangered by foreign bribery. When foreign payoffs are concealed a corporation cannot give a true financial picture of its financial position to prospective investors, stockholders, underwriters, brokers, and to the government. Such practices can only be concealed through devious accounting methods (for which the revised bill proposes to give an opportunity with the term "material") that endanger the credibility of the corporation both at home and abroad. One can hardly visualize a corporation ever including in its financial statement or its reports to its stockholders that such and such foreign bribes have been given. Although most stockholders are interested chiefly in maximum financial returns on their investment, still it would be a great indictment of the American people to say that they do not care how these financial returns have been achieved.

6. Foreign bribery produces unfair competition between those U. S. corporations that do bribe and those that do not. It is quite important to realize, moreover, that U. S. corporations compete against each other to bribe foreign officials to secure sales. It is my understanding, incidentally, that bribes to gain advantage over other U. S. competitors also constitute a violation of anti-trust laws. Competing corporation bribes do not add to the U. S. balance of payments when the sale would probably have gone to a U. S. corporation anyway. The added costs of the bribes establish a pattern for future U. S. corporate sales in a given country.

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In fact, many corporations have successfully sold our products overseas without paying bribes. As Sorensen stated in relation to improper payments abroad, "Those governments desirous of obtaining U. S. technology and quality will unquestionably learn to buy our goods without any special inducement."

7. It is illogical to exempt foreign bribery where "customary," and it endangers the entire system of control over bribery. The proposed amendment to the existing law exempts "any facilitating or expediting payment to a foreign official which is customary in the country where made and the purpose of which is to facilitate or expedite performance by such foreign official of his official duties." This position is both illogical and dangerous. Such an exception would seriously endanger the entire system of control over foreign corporate bribery. To follow this assumption to its logical conclusion, moreover, a host of corporate business practices in this country would be exempt from the law because they are "customary" ways of doing business. Among such practices are corporate political contributions, commercial kickbacks, false and misleading advertising, polluting the environment, and many other common business practices.

Who is to say, furthermore, what is customary in a given country? Certainly not all public officials in any foreign country can be bribed. The legal codes of virtually every nation in the world prohibit the acceptance of bribes by their officials. Under these circumstances it is highly misleading to assume that bribery is "customary" without recognizing at the same time that any official who accepts such bribes is violating the laws of his own country.

The arguments against foreign bribery and in support of the present law can be summarized as follows: (1) Foreign bribery represents an inconsistent attitude between foreign and domestic business activity, (2) foreign bribery ^{may} negatively affect foreign governments and tarnishes the

image of the United States abroad, (3) foreign bribery negatively affects the developing countries, (4) foreign bribery may be injurious to the corporation itself, (5) foreign bribery endangers the credibility of corporate financial statements, (6) foreign bribery produces unfair competition between those U. S. corporations that bribe and those that do not, and (7) the exemption of foreign bribery restrictions where it is customary is not only illogical but it endangers the entire system of control over bribery.

The Foreign Corrupt Practices Act appears to have corrected a serious problem; likewise, it seems to have operated quite successfully. Our non-agricultural exports have not materially suffered, and in cases where they have been affected it has, in all likelihood, been due primarily to other causes. Virtually to scuttle the present law, as certain clauses in the proposed amendment actually do, with the hope of obtaining additional financial returns by certain corporations, is not in accordance with my conception of the proper role of the United States in the turbulent political world of today.

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Mr. WIRTH. Thank you, sir.
Mr. Akins?

STATEMENT OF JAMES E. AKINS

Mr. AKINS. The Foreign Corrupt Practices Act was designed to end bribery of foreign officials by Americans. Whether it adversely affected foreign trade is questionable. Mr. Rinaldo has suggested that a number of American companies have maintained that it does. I have frequently heard that complaint myself. Mr. Eckhardt gave figures showing an increase in our trade in the last 10 years. He said that he does not claim that the FPCA is responsible for that increase, but perhaps he is being a bit modest. It might indeed have helped increase trade.

There is no society in the world where corruption is condoned and certainly not by any religion. Corruption allegedly is rampant in the Middle East but the prophet Mohammed said, "God curses the briber and the bribe."

Soliman Solaim, the Saudi Minister of Commerce, has consistently told American companies that they should be proud of the act, that it sets them apart from other companies and other countries. He said when the Saudis deal with American companies, they know that because of this act the companies must be honest, and that they cannot give bribes to local officials. He says, "We can't be sure about other countries and other companies."

There is no doubt that many American companies working abroad think it is customary to bribe foreign officials. Whether it is or is not if a company believes it is, it will always be able to find a local agent who will take its money. Whether the agent would be able to do something for the company is something else.

A common technique I have seen used in the Middle East is for a would-be agent to learn through his sources in the government which foreign firm is in line to get a contract. He then goes to this company and says: "Look, you are in deep trouble. You are not going to get the contract; you have no chance. But I can help you. You don't have to pay me anything if you don't get the contract, but you pay me a large sum if you do." Companies tend to fall for this ploy. The "agent" has done nothing for the winner—but he pays the fee. Ahmad Zahi Yamani, the Oil Minister of Saudi Arabia, has tried to keep oil sales from his country clean. He says "We keep our books open and make sure everybody knows the Saudi Treasury gets \$32 each barrel of oil it sells. We can also make sure the criterion for giving oil contracts is well known. But if a foreign company decides it wants to pay an agent \$2 or \$3 a barrel for doing nothing, there is nothing we can do to protect this company from its own stupidity."

There is no point here in putting up a straw man and knocking it down. We have heard some companies say the act must be repealed but I am pleased to learn here that there is no intention of changing the basic thrust of the act, which is to prohibit bribery of foreign officials. However, the act was drafted by human beings and like all human actions is not perfect. Perhaps it does need a few changes or at least a formal reinterpretation.

Mr. Eckhardt testified that the law did not apply to the "mordita," to the small payment, the small local official who is "greased" to get something through Customs, to get an export permit, or a residence permit. Such petty corruption will exist for as long as foreign officials are grossly underpaid, as they are in many Third World countries. There is nothing that we can do about that. I have heard some American companies complain that the act does apply to such payments. If it does not certainly there should be some clarification.

A more important complaint pertains to the use of agents. The act is quite explicit in forbidding the use of an agent in countries "where bribery is known to be common." Unfortunately it is very difficult to know or prove where bribery is "known" to be common. And companies feel inhibited in doing business through agents.

That could probably be corrected by specifying in the act or in the revision or in the interpretation of the act that the agent's fee be known, that it be included as part of the contract. If it is known, then the local government can make its decision on whether the agent or his fee is to be paid or not.

I do not think there is any government in the world that would publish a 30-percent payment on a \$1 billion contract. There is no country in the world that is so stable that they could allow its people to know that such payments were made.

If a modest agent's fee is paid, and the country involved does not object, then I see no reason why it should be prohibited—even by implication—in the law.

Agents are useful in many countries, but not all. They are forbidden in some countries. Iraq is a good example. The position taken by Iraq against corruption has been the most severe in the Middle East. A Deputy Minister of Irrigation was recently executed for taking a bribe, of \$10,000 from an Englishman. The fee was very low by general Middle East standards. An Araq Army officer was executed for accepting a gift of \$500. There aren't many executions elsewhere, but bribery and corruption are as illegal in all of the countries in the Middle East as they are in Iraq. The punishment is just more severe in Iraq.

I would hope in the reexamination of the act that its basic intent is kept intact, and that any changes or any reinterpretations that are made do not imply to any foreigner or to any American company that we are now less opposed to bribing them than we were when the act was passed.

[Mr. Akins' prepared statement follows:]

TESTIMONY BEFORE THE SUBCOMMITTEE ON TELECOMMUNICATIONS, CONSUMER
PROTECTION AND FINANCE
OF THE
COMMITTEE ON ENERGY AND COMMERCE

OVERSIGHT HEARINGS ON THE FOREIGN CORRUPT PRACTICES ACT OF 1977
Held at the Rayburn House Office Building, Washington, D.C.
September 16, 1981

James E. Akins, U. S. Ambassador, ret.

I arrived in Saudi Arabia in 1973 during the last Middle East war. Since 1951, I had worked in and with various countries of the Middle East where payments by businessmen to local officials were widely known and discussed. In the telling and retelling of these stories in the Middle East societies, the size of the payments was generally exaggerated. Nonetheless, they were frequently substantial, particularly when made in connection with military sales. "Agents' fees" of up to 30 percent of the gross cost were reported to have been paid in connection with European arms sales to Saudi Arabia and elsewhere. Payments made by the American arms companies were generally rather less but we know from documents obtained by the Senate in connection with hearings which led to the passage of the Foreign Corrupt Practices Act that they were at times as high as 20 percent.

Most of the American arms sales have been made through official American channels (the Foreign Military Sales program). The Saudis told me in 1975 after the payoff scandals broke in the American press that they had assumed no agents' fees were included in these deals. Prince Saud, now the Foreign Minister, told me that avoiding the payment of agents' fees was precisely the reason the Saudi government used the government-to-government method of procurement. I did not take this entirely seriously at the time; it seemed to be a degree of naivete that could not be ascribed to that highly intelligent and educated Minister. The Saudis were nonetheless quite consistent on this

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point. Prince Sultan, the Defense Minister, said in a newspaper interview, published on September 7, 1973 (al-Hawadess; Beirut, Lebanon):

"When we buy arms, we insist that the determining the specifications and the fixing of prices should be under the control and supervision of Saudi military experts. Once the phase of concluding the contract is reached, the contract is executed between the governments concerned. No deal is ever closed with a broker. If some arms companies are bound by agreements with agents and pay agents under these agreements, regardless of their role in concluding the contract, this is a matter that concerns the seller; we have nothing to do with it. It does not affect our freedom in concluding the contracts. This rule is applied in all commercial operations, whether in connection with arms equipment or otherwise."

There were good reasons for their believing this. Agents' fees were never identified in the FMS cases. Whatever the fee was, it was concealed in each line item; that is, every item on the sales contract was increased by the agents' fee. Documents released by the Northrop Aircraft Company in connection with the original hearings on this bill claim that the American Ambassador to Saudi Arabia told Prince Sultan in late July 1971 that there was no agent's fee on a particular contract when, in fact, there was a substantial one. I have never seen pertinent State Department documents on this matter, nor am I sure there are any. Ambassador Thatcher, who retired in 1973, was questioned by telephone on this, according to testimony of Deputy Secretary of State Ingersoll on March 5, 1976, and recalled "no knowledge of Northrop's agents arrangements at the time the Letter of Offer was signed."

My objection to such payments was ascribed by some to an excess of puritan zeal and, while I cannot totally deny the effects of a Calvinist childhood, I believed (and still believe) that massive payments to agents and bribes to foreign officials destabilize the countries where they are being paid, that they are unworthy of the United States, and that they basically are unnecessary.

Shortly after I arrived in Jidda, I spoke with heads of all American companies who asked me about this issue and many who did not ask for my opinion.

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I told them all that they should make no irregular payment to any Saudi in connection with any contract, military or non-military. If they were asked for such payments, they should inform me and I would take it up with the Saudi government. At the same time, I discussed the matter with Sayid Omar Saqqaf (then the Saudi Foreign Minister), Prince Sultan Abd al-Aziz (the Defense Minister), Prince Fahd Abd al-Aziz (then the Interior Minister) Ahmad Zaki Yamani (the Minister of Oil) and Hisham Nazer (the Minister of Planning). I told them what I had done with the American companies was basically for the good of Saudi Arabia; they would benefit through lower costs and better performance and although Saudi Arabia was rich, their money would be used more wisely. They all agreed. I told them that, having taken such a position, it would then be intolerable to the American companies, to the American government and, most importantly, to me personally, if American companies would lose contracts to Europeans or Japanese who had no such restrictions and over whom I had little influence and no control. All the Saudis lauded the position in the strongest terms and all said that if such a case were brought to my attention they would take it up immediately with King Faisal and the matter would be settled.

It is impossible to affirm absolutely a negative; that is, I cannot state categorically that no payments were made for any new contracts signed while I was in Saudi Arabia. One must assume (knowing the position I took on this matter) that if a company concluded that the only way of getting a contract was through payment of a bribe or a large unannounced agent's fee it would not have brought the matter to my attention. But there are no permanent secrets in the Middle East and I am confident that I would have heard about

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any such action - particularly if the payment had been a large one. During this period, the remainder of 1974 and all of 1975, American business flourished in Saudi Arabia.

It is frequently stated in opposition to the FCPA that corruption is endemic in much of the world and the United States is blind not to recognize this fact. It would be foolish to deny that irregular payments are made in many countries of the world. I should emphasize here that I am not referring to payments of a few dollars to minor officials to expedite clearance through customs, to get visas, or work, residence or exit permits. The sums involved are not large and, as long as civil servants are grossly underpaid in underdeveloped countries, it will probably be impossible to avoid such payments. Some American businessmen believe these payments are forbidden under the FCPA and, although I am not aware of any prosecutions having been made for such payments and I am convinced that such payments are being made, the law probably should be amended or explicitly reinterpreted to make clear that it does not refer to such minimal payments. Definition of "minimal" will not be easy and perhaps it would be desirable to make an absolute prohibition against all "irregular payments" (morally a case could be made for this) but such a rigid position would ignore practices in much of the world and would unfortunately but clearly inhibit business activity.

A major section in the law in connection with agents' fees is perhaps the most troublesome from the point of view of the businessmen. The law provides that if the American company has reason to believe that the agents' fee might be used for bribes or if a large agents' fee is paid in a country where bribes are habitual, that no such agents' fee can be made. Proving what is

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"habitual" or what a company might suspect is extremely difficult to demonstrate and, although I know of no cases where there has been prosecution under this section of the act, I do know that companies are inhibited in doing business because they think they need agents. In many but certainly not all countries they do need them, and they are invariably well paid. The problem of the size of an agent's fee is bothersome to many companies. Most governments oppose large fees and Iraq at least forbids payments to Iraqi agents. This matter could be handled by specifying that in all contracts signed by Americans, the agents' fees must be identified. If the local agent or the local government objected, it would be a clear signal that the fee was to be used for improper purposes. It would be difficult, if not impossible, to determine an absolute maximum on an agent's fee or even to determine the propriety of such fees; they would depend on circumstances in the country and the size of the contract. It is unlikely that many countries (even one as rich as Saudi Arabia) would tolerate an announced agent's fee of 10 percent or even 5 percent on a multi-billion-dollar contract. Most governments would prefer that the contract be reduced by that amount and would probably insist that this be done, even if a high government official were the agent. The public scandal in connection with some agents' fees, even if an attempt is made to conceal them, is great. If the fee were formally announced, it would not be allowed. Of course, it will be argued that if Americans do this and others do not, business would be lost. But the American company and the American Embassy would be in a position to make representations to the local government if the American bid were lowest and the award went to another firm.

In many cases businessmen are deluded into believing that it is necessary to make payments when in fact it is not. Quite frequently an unscrupulous

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agent, who invariably has nothing to do with the decision-making process in his country but has access to someone who does, learns of his government's intention to give a contract to a specific firm. The agent then goes to the firm, tells it that he can make arrangements for it to win the bidding, even alleging that the firm has already been excluded from consideration. His pitch then seems reasonable: the firm need pay him nothing if he does not succeed in getting it the contract. All too frequently, the company officials panic; they agree to the agent's conditions, and they pay him a large fee when the contract is awarded. Although he has performed no service at all, they do not know this. An excellent example was an oil deal signed between the Italian oil company ENI and Saudi Arabia in 1979. The Saudis had befriended an Iranian, Parviz Mina, who had lost his job as head of the National Iranian Oil Company after the overthrow of the Shah. Mina was employed by the Saudis as a consultant and he knew, as did many others, the method used by the Saudis to allocate oil contracts. Mina saw that the time was propitious for the Italians to get a contract, particularly in view of a planned trip by the Heir Apparent, Prince Fahd, to Italy. Mina, according to Italian documents, told the Italians that he could arrange the oil deal for them in return for a payment of 7 percent into a Swiss bank account. This amounted to some \$200 million over the three-year life of the contract. Mina had done absolutely nothing to get the contract but the Italians believed that he was responsible and payments totalling about \$18 million were made on a few shipments. The Italians who were in no way disturbed by payments to be made in Saudi Arabia (they thought that this was the way of doing business there) did object when they concluded that part of this money was diverted to the

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pockets of Italian politicians. The scandal then broke in the Italian press. The Saudi position was precisely the opposite: if the Italians wanted to pay more for their oil and give the difference to Italian politicians, that was their own business. But paying agents in Saudi Arabia for Saudi oil was against Saudi law. The contract was cancelled.

If a foreign company wants to find someone to take its money, it will find that the country - whatever it is - is not short of candidates to do so. Adnan Khashoggi, one of the most notable of the agents in the Middle East, has testified that he did indeed take Northrop's money but he used it for himself; he did not pass it on to any Saudi officials. This could well be true.

When the Northrop case broke in 1975, I was in the United States on leave and, as it turned out, in the process of being fired. Nevertheless, I was asked to return to Saudi Arabia urgently to take the matter up with the Defense Minister and with the King himself. Contracts had been signed by Northrop with Adnan Khashoggi in California; they provided huge payments to Khashoggi for every sale Northrop made in the Middle East, whether Khashoggi did anything for them or not. The contracts were well drawn up, simple, and hence hard to break. Had Northrop made these payments to Khashoggi, without recouping them from Saudi Arabia, they would have been larger than the global annual profits made by the company. The Saudis had no intention of making payments which, they said, they had been led to believe did not exist. I took this up with the Minister of Defense and with the King. A Royal Decree was issued explicitly forbidding the use of agents on military contracts. The Defense Minister or some high government official apparently also told

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Mr. Khashoggi not to press Northrop. He did not pursue the matter at the time although the sums of money were staggering. I understand in the last year his case against Northrop has been reopened.

The largest contracts in Saudi Arabia - those carried out by Bechtel and by the four major American oil companies who comprise ARAMCO - have been concluded without a breath of scandal. The very extensive military and civilian contracts supervised by the American Corps of Engineers have also been above reproach. There was never a suggestion of payments from the Saudi side and never an offer by the Americans.

In many parts of the world the American ambassador has very strong if not pre-eminent position, and support of a company by the ambassador can be valuable. I am convinced that in many cases attempts at bribery or corruption could have been handled quite effectively by an appropriate intervention of the ambassador on behalf of the American company, particularly when unscrupulous agents claim payment for services they do not and cannot perform. When it was revealed that a major oil company had made considerable payments in Korea, I told the company president that this seemed to me to be extraordinary; Korea is surely amenable to American pressure; surely the American ambassador could have taken the matter up with the Korean President and ended the pressure for kickbacks. The company president replied that not every American ambassador took the same view on the subject that I did. This may be true but he did not try; the American Embassy in Seoul was not informed of the pressure and therefore the ambassador was in no position to intervene on behalf of the company.

If the FCPA is amended, or reinterpreted - and perhaps some of the more sweeping sections should be - I hope that its essential purpose remains intact.

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Apart from petty graft which probably cannot be controlled, the main purpose of the legislation is to stop large, unofficial payments or bribes to foreign officials. I suggest that this has helped rather than hurt American business as a whole. As long as the law is on the books, any American company and any American ambassador can insist that his company is behaving in an absolutely honorable way, that any bid made for a project in the country is an honest one, that it is the lowest price that can be offered, and that if other companies make higher bids/through payments of kickbacks, then the company and the American government have legitimate complaints. There are governments in the world which are so corrupt that they could dismiss an official American government protest on such a matter and would try to suppress all word of such protest. But there are not many governments, and I am convinced that those which are so venal will face internal unrest and revolution. Generally, if the public knows that a contract is given to a company because of kickbacks, the hostile reaction could be quite dangerous to the government - any government. There are few governments that are so firmly entrenched that they can totally ignore the will of the people.

It is sometimes stated that different cultures look differently on bribery and corruption than do we. I have heard the charge that Muslims particularly are unoffended by corruption. This is totally untrue. The Koran is explicit in its condemnation of corruption, and no Islamic country or society condones corruption, morally or socially. We should not forget that corruption (along with offenses against human rights) brought down the Shah of Iran; that corruption was an important (if not the major) reason for the revolts against King Farouk of Egypt and King Idriss of Libya. There are corrupt officials in most countries, including our own, but no moral or social system approves bribery.

No foreign government can object to the FCPA; many governments would in fact welcome it as beneficial to themselves. Even if foreign officials see the loss of bribes and kickbacks, they could never use this as an objection to doing business with the United States; it would be a tacit admission of openness to bribery. Rather than asking for abolishment or weakening of the act, I hope American companies working with American Embassies, will look more completely at how the FCPA can be used to their advantage and to that of the countries where they are operating and ultimately to the benefit of the United States.

Mr. WIRTH. Mr. Blum.

STATEMENT OF JACK A. BLUM

Mr. BLUM. Mr. Chairman, in your invitation you asked about the factual origins of this act.

I would like to go back to the real origin which was the Watergate investigation.

We discovered that there were hundreds of corporations that made illegal domestic campaign contributions, and as the Watergate prosecutors went through the books of those companies they discovered off the books accounts and could not understand what the rest of the money had gone for. They began to realize it had gone for overseas payments of one kind or another, which then in turn led to the SEC investigation, which in turn led to the various Senate investigations.

The Senate investigations began with some of that information but then carried on to a much wider field.

The discoveries were that bribes were not limited to facilitating payments. Bribes were not limited to harbor masters but indeed could go to the heads of state of Western governments presumably in the civilized world which came as quite a shock to a number of Members of Congress who always believed that this behavior was confined to the Third World where they thought it was appropriate because of foreign competition.

My concern with this problem is first and foremost the national security concern. The United States cannot afford to have corporate bribery undermine U.S. national security.

When I went to work for Congress there was a security check of my background. People insisted on knowing whether there was anything in my background that subjected me to blackmail. If I had been bribed somewhere in the course of Government service, I would have been subject to blackmail.

Messages are intercepted constantly. If you go back through the records of the hearings you can see that the bribes were very badly concealed by espionage standards, and I am certain that any high official who received a bribe was made vulnerable to foreign blackmail by the fact he received the bribe.

We cannot permit that to happen. There is a second national security aspect of this.

We undermine our own national security objectives. We have to sell various foreign governments on the notion that they have to protect themselves. They have to have a military budget, they have to buy a piece of military equipment. If the companies selling that equipment pay bribes to the heads of state, there is no way we can convince the foreign government or the people of that country that what we want is really legitimate and not a way of raising money and selling weapons.

We also undermine our friends in those countries. When Prince Bernhard was paid by Lockheed we lost the credibility of a very good friend of the United States in the Netherlands. Bribery in many countries in the world is a way of life, and there are many parts of the world where it is assumed to be a way of life, but ulti-

mately when the bribery reaches circus levels the government falls and the U.S. national interest is utterly destroyed.

The progression in the Middle East, makes the point. In Libya, where American companies engaged in wide open bribery, King Idris, a friend of the United States was followed by someone who is quite inimical to American interest, Mr. Qadhafi, and one of the strongest forces which brought him to power was the fact that the government that preceded him was utterly corrupt.

The case of the Shah has already been mentioned. Hopefully, as a result of this act and earlier disclosures, the situation in Saudi Arabia is now under control. The notion that we would permit American companies to participate in this behavior without some attempt to control it in my judgment is the height of national folly.

I believe that we cannot accept the act as it is, that as it is, it can't possibly be enforced. To understand my point you must go back to the Lockheed affair in Japan. Had a Lockheed official been indicted for bribing a Prime Minister of Japan, we would have been confronted with an absolutely impossible foreign policy situation, and we would have had to have given up the prosecution.

You cannot indict an American for bribing a foreign official and then give the foreign official no way of defending himself, which is, of course, what would happen. In my judgment we have to find other ways of curbing this bribery, and the system that I submit would be the best was the proposal raised by the Ford administration, which is a form of disclosure. Rather than bore you with details on how that might work, I would be prepared to discuss it with the committee and staff at your convenience, especially when you turn to writing your legislation.

I think finally a point that was made before has to be underscored. This is an issue which is vital to the security interests of the United States.

There is no question in my mind that other governments, and I can tell you from personal experience having investigated extensively in Europe, that other governments and other governments' companies are very much involved in this issue.

The United States never really at a very high level sat down with its allies and said, gentlemen, unless we curb this business we are going to destroy our own collective security. We are going to destroy our NAT Alliance and find it impossible to keep military secrets. We have much at stake, and we will endanger our resources. We have never raised it to that level, and we should, and I think that if we do, we can begin to get some form of international agreement which will get this issue under control.

I think that competitive question is the one that most concerns American businessmen who say we are curbed and they are not. I think that is a matter for international negotiation, and I think the negotiation can be undertaken.

One final point, and that is the question of the involvement of the U.S. Government.

All too frequently it has been easy for our Government to turn a blind eye to what is going on in a given country and act as if it does not know. In Iran everybody knew what was happening, but officially the U.S. Government acted as if it didn't know.

I think that that is something that is the place of the American Ambassador in the country and the various other Americans in official capacity to take note of and call companies to task and raise the issue because so much is at stake for the country as a whole.

Thank you.

[Testimony resumes on p. 100.]

[Mr. Blum's prepared statement follows:]

STATEMENT OF JACK A. BLUM

My name is Jack Blum. I am a partner in the Washington, D.C. law firm of Blum and Nash. Before entering the private practice of law I was on the staff of the Senate Foreign Relations Committee where I worked on the problems of questionable foreign payments by U.S. corporations. I have also served as a consultant for the United Nations Centre on Transnational Corporations on the issue of corrupt payments.

The Foreign Corrupt Practices Act is under sharp attack in the business community. The harshness of its criminal penalties, the lack of realism in addressing international competition and the vagueness of the language have all been properly raised.

In my opinion the Act is flawed in concept and should be revised, but there is no question that legislation in this area is essential to the protection of the security interests of the United States in its rivalry with the Soviet Union, and is necessary to protect the position of the United States in its relationship with Third World countries which provide the raw materials, energy resources and markets for the industrial sector of the economy. Moreover, and from a personal standpoint, most importantly, legislation is necessary to protect the integrity of our own political processes.

I am sure that this Committee is familiar with the volumes of testimony and documents the Foreign Relations Committee published during its investigation. The testimony, especially the testimony of the officials of Lockheed, illustrate the national security issues I wish to raise.

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Before taking my job with the Senate I was required to undergo an extensive background check as part of the security clearance process. Our government, quite properly, wanted to know whether I had done anything which would make me subject to blackmail. If a foreign government's spies can find vulnerability in an official with access to classified information they can and will exploit it.

According to documents in the Senate hearing record, Lockheed made indirect payments to various high officials in Italy to assist in a military sales campaign. At least one of those officials was privy to top secret NATO defense information. Lockheed representatives communicated with each other and with their "agents" with all the sophistication of two ten-year olds sending each other messages which could be decoded using the "decoder" ring in a cereal box.

I must assume the KGB is at least 50% as effective as we are in intercepting messages and that there is a high probability that even if the Italians or the Americans never found out about the payoff the Russians would have, and by finding out could instantly recruit a high level agent with access to critical defense information. The payment thus undermined NATO security.

Consider another of Lockheed's payments - its money to Prince Bernhard of the Netherlands in connection with the sale of fighter planes. The United States must put continuing pressure on the Dutch government to get it to maintain an adequate NATO contribution. The Dutch government always seems to prefer using

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its money for social programs rather than defense. The bribe to Prince Bernhard undercut the ongoing political efforts. The Dutch could and did rightly ask whether the weapons system we were pushing had any real purpose other than creating arms sales and cash flow. The arguments of the arms salesmen were portrayed as simple greed and discredited. Worst of all the personal credibility and image of one of America's best friends in Holland was destroyed completely in the wake of disclosure.

During the hearings, our Committee was accused of creating the problem by disclosing the payments. In fact, as you all well know, disclosure can and usually does come from political opponents, foreign agents, disgruntled employees, scorned lovers, and the press rather than Senate or House investigations.

The United States must have the ability to control this behavior and to stop large high level payoffs if it is to protect the national security.

It is axiomatic that high level corruption undermines governments. All of the cant about "bribery as a way of life" falls apart when it is applied to the highest levels of any government. In both the developed and the developing worlds in Europe, Asia, South America and Africa high level bribes are unacceptable. The government of Japan was paralyzed for six months over the possibility that a prime minister had been bribed by Lockheed. If in fact the behavior was socially acceptable the reaction would have been momentary. Fidel Castro owes his power

to the corruption of the government of Batista by outside interests.

If you have any doubt about this issue and its importance to the United States, consider the way in which American business has dealt with a number of countries in the Middle East and the events which followed.

It is widely known that the Libya of King Idris was a circus of corruption. Stories of how oil concessions were obtained are now legendary. The circus continued for several years, oil flowed and business was good. Then from nowhere Mohamar Kaddafi took power. He was a totally unknown army officer and he was able to drive the corrupt king from his throne calling himself the righteous avenging sword of Allah.

His first moves were to cut production and raise oil prices. His next moves were sponsorship of international terrorism and regional destabilization.

Iran became the next major focus of business interest. As revenues increased, it became apparant to one American firm after another that the Shah was a technology nut and that with the right set of agents paying the right set of generals almost any piece of equipment could be sold.

In the cold dawn of the regime of the Ayatollah Kohmeni, we should reflect on how the payments in Iran weakened the Iranian military, destroyed the Shah's support among students and incurred the wrath of religious fundamentalists. Our failure to

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show more restraint in Iran and to encourage our allies to show more restraint had a fearsome price.

Saudi Arabia has a stunning similarity to Iran and Libya. Its monarchy weathered the storm over the disclosure of huge commission payments but it continues to be vulnerable and its vulnerability is the most important national security problem we have. The economic health of the west depends on the continuing flow of Saudi oil.

To the extent that we have an interest in international stability, in good economic relations and in the success of our own democratic process, we have an interest in preventing our firms from making high level, corrupt payments.

When payments are disclosed, the citizens of the country involved cannot differentiate between the company that made them and the United States government. For example, when fruit company bribes in Honduras were disclosed, the American Embassy was the target of demonstrations.

Further, once patterns of payments and machinery for concealing them are established, corporations have tended to forget the distinction between foreign governments and our own. Gulf Oil, for example, used its Bahamian subsidiary for both foreign and domestic payments. If off the books accounts are available they will be used here as well as abroad. The very investigation of foreign payments grew out of the files of the Watergate prosecutors who discovered large corporate off the

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books accounts but found that Watergate and CREEP contributions accounted for only a portion of the money.

There is no way to quarantine improper behavior if the controls on hidden accounts are repealed. Ultimately, some of that money will return to our society.

What then is the answer?

My work at the United Nations and my experience with the realities of life in much of the developing world have convinced me that criminalization of certain foreign payments was a mistake and that the Act as it stands is fatally flawed and unenforceable.

Consider the following hypothetical case: a major corporation is caught red-handed trying to bribe the prime minister of Japan. The evidence is clear and a grand jury prepares to indict the offending corporation and its officials. The question then is what will the political reaction be in Japan?

The moment the indictment is returned, the Japanese prime minister will, de facto, be a party to the case, whether he likes it or not. His career and his political party will rise or fall on the results of the trial.

He cannot defend himself. He cannot be represented by counsel and as a practical matter he cannot give up governing and subject himself to an American Court's jurisdiction.

There is also the real possibility and indeed the presumption that he is innocent. After all, most people who pay

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bribes don't ask for and get receipts and it is entirely possible that even if the corporation intended to pay the bribe, set up the machinery, and disbursed funds, the Prime Minister never saw them because the intermediary pocketed the money.

In fact, Adnan Kashoggi tried to protect the integrity of the Saudi royal family by saying that he pocketed hundreds of millions of dollars worth of commissions from Lockheed and Northrup and in other cases it was clear that the middlemen "deducted" substantial portions of the payments.

Yet, it is just the sort of high level pay off that the U.S. government must prevent and against which the law is ineffective.

Although I have raised the most difficult political problem, consider a few of the others. Much of the evidence in a case such as this will be outside of the jurisdiction of the United States.

- . Can this country ask a foreign country for help in getting evidence which will indict a corporation for bribing its own leadership? Each request for evidence will become a matter of grave foreign policy concern on both sides.
- . Will prosecutors be accused of meddling in foreign elections and partisan politics if investigations coincide with important political events?

If these problems sound difficult I can assure you that they are. I lived through the disclosure of the Lockheed Japanese payments and the many complex problems giving the material to

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Japanese prosecutors engendered. A special judicial assistance agreement was reached after extensive negotiation, but U.S.-Japanese relations turned on this issue for a long time.

I cannot imagine what would have happened in Japan if we had gone ahead with a trial of the Lockheed executives for violations of the Act if it had then been in place. My best guess is that our president would have dropped the prosecution for national security reasons and would have been justified in doing so.

Apart from the difficulty of prosecuting violations one must face certain realities of the international businessmen's world. Other countries' major corporations do the same thing, sometimes in a fashion more flagrant and dangerous than any American corporation would dare. As I travelled Europe collecting information on U.S. corporate activity, I heard endless stories about the French arms manufacturers. How they sold tanks here and planes there even though the tanks were marginal and the planes were a generation out of date. Although I had no hard evidence, the number of different people around Europe who told the same stories convinced me that the French arms merchants were not the moral giants of the business world.

These are the people our companies must compete against if they are to succeed, and we cannot act as if the foreign companies play fair.

Also, in some countries routine business cannot be done without facilitating payments. Some harbormasters won't let a ship unload until they are paid. In Indonesia a simple telephone

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call from one island to another requires a gratuity and in parts of Latin America a border crossing without a payment is a major ordeal.

I believe these problems must be faced squarely without either childish moralizing or a "boys will be boys" dismissal.

The competitive problem is an issue for the entire Western developed world. The questions I have raised are present for every country which is the home of a major international corporation or which exports expensive, high technology equipment. Each of them must ask whether they are willing to risk their own national security to make a sale or whether they wish to allow a resource rich country upon which they and their allies depend to become destabilized through the corrupt actions of their businessmen.

I believe that if these questions are raised directly and forcefully on a government to government basis then there can be negotiated solutions among the OECD nations. The high pressure competition for multibillion dollar sales can be kept under control and a few fundamental rules can be established. To make a system of negotiated communal refusal to compete through payoffs work, governments must know what is going on in the marketplace and must raise the issue of improper behavior with other governments.

Reaching agreement on this issue is fully as important to the collective security of the West as weapons systems and

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military budgets and must be treated on the same level of importance.

Facilitating payments are properly issues for the host country governments to address. They have full jurisdiction over the actions and the evidence and the payments do not so affect the national interest of the United States that legislation is required. If a businessman abroad wishes to make the payment locally it is his affair and his risk.

The legislation this committee develops should enable businessmen to operate, yet at the same time, protect the national interest by keeping their behavior within bounds. In 1976 the Ford Administration suggested a disclosure program as an alternative to criminalization. The idea has merit and should be revived.

Corporations should be required to disclose all payments over a minimum threshold amount to foreign officials, including officials of state-owned companies, foreign political candidates and foreign agents. The purpose, amount and recipient of the payment would be reported to the Departments of State and Justice. The information would be treated as proprietary and not subject to Freedom of Information Act requests, unless the U.S. government chose within a stated time period to enjoin the actions and the payments on national security grounds. Before seeking a court order, the U.S. government would be required to discuss the issue with the company involved to see if it can be persuaded to change its behavior. If an agreement is reached,

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the entire process would remain confidential. Failure to disclose would result in civil penalties, willful failure in criminal penalties.

This system would force a dialogue between the companies and the government on the issue of payments. Our government would have to pay attention to competitive situations involving bribes by foreign companies and would have to assess security risks and weigh the competitive problem. It would have to note particularly corrupt foreign business settings and would have to bring those problems to the attention of foreign leaders forcefully. It would also have to raise the issue with other governments whose companies are participating in the corrupt environment.

Disclosure would also end the ambiguities in the present law which the corporations say they cannot live with. There are simply no fine distinctions to be made under a disclosure system. Either a transaction is to be reported or it isn't.

The legislation should make plain in its preamble that the issue is protection of the U.S. national security and the U.S. interest in peace and economic stability, not the enforcement of American morality abroad.

Any foreign government wishing to clean up its own act should be encouraged to do it. To that end the United States should renegotiate its largely outdated judicial assistance and extradition treaties with foreign governments to make it possible

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for them collect evidence and to pursue people who have corrupted their governments.

Disclosure requirements must be backed up by corporate accounting requirements which prevent the establishment of "off the books" accounts. A fine tuning of the existing law with this objective in mind would be appropriate. The recommendation of the General Accounting Office to decriminalize violations other than willful falsification should be followed. We should remember that these provisions are important for keeping improper payments out of our own political system as well.

The shift to a disclosure approach would solve the problem of trying to hold a high corporate official criminally responsible for acts of which he "had reason to know". Although many of the bribery cases involved corporate approval at high levels, others did not. In some cases, the payments were reported to high level officials but dressed in a way which hid their true purpose. In other cases payments came through joint ventures or in forms that made the issue of top level management involvement and control very difficult to determine and at best debatable. Criminal prosecution on the reason to know standard is a questionable constitutional proposition.

The revision of this law should not be used to preclude prosecution of related acts under other laws such as the Federal Trade Commission Act, the Internal Revenue Code, the securities laws and the mail and wire fraud statutes. Those laws have different purposes and are either legitimate in their own right

or should be repealed. Indeed, sweeping these laws off the books where foreign payments are involved would turn a new statute into one which facilitated bribery rather than curbed it.

In my experience few issues have as many sticky sides as this one. No corporate president will be seen testifying frankly at a hearing on the subject. None of them want to publicly discuss the subtle shadings of the issue and be exposed as "immoral" even though the issue is not totally clear cut. Similarly, most diplomats would rather pretend this issue doesn't exist because recognizing it forces the diplomat to see some difficult and uncomfortable problems and become a responsible participant in the actions of his countrymen. Can a diplomat admit he knew what was going on and did not report it? Or worse still, can he admit that even though his job was knowing all about the commercial climate in a given country, he did not know what was really going on?

It is time to write legislation that ends the morality charade and forces company officials and diplomats to say some hard things to each other, to our allies and our competitors so that we don't all destroy the system we are working so hard and paying so much to defend. In the process we will find that our own political system will also be protected.

If you have any questions I will try to answer them and I will be more than willing to work with the Committee and its staff on drafting new legislation.

Mr. WIRTH. Thank you very much.

Some of you might want to react to what others have said.

Does anybody want to do that?

Let me start if I might by asking you, Mr. Hills, to respond to what Mr. Blum is suggesting. If I understood your suggestion, Mr. Blum, that disclosure is the key to all of this.

Is that similar to what you are suggesting?

Mr. HILLS. Yes, it is the same remedy. I must say that I was proud to be a part of the Ford administration, and that specific proposal that came out of a subcommittee or task force with respect to disclosure struck me, and I think many of us at the time, as quite cumbersome.

The disclosure that exists now, certainly with respect to publicly held companies, I think accomplishes what Mr. Blum is seeking, namely, sufficient exposure of corporate activities to outside auditors, outside directors, to Government surveillance, if appropriate, to the IRS and elsewhere, to provide the kind of governing system to prevent the kinds of gross bribery that we found during that period of time.

There is a problem with a privately held company that does not report publicly and admittedly a disclosure system would need to be developed for a privately held company in the event that the criminal penalties, as they are now appended to the act, were substantially changed, but I think, given the scrutiny of the IRS and the fact that all companies of any size must go through that process, finding a method of comparable disclosure for a private company, is not an insurmountable barrier.

In other words, we have an enforcement procedure, a noble and able capacity, with respect to the scrutiny and the governance of the publicly held company and the same kind of system can be created and built on the IRS for a privately held company.

Mr. WIRTH. Do you all agree that that is the basis on which this legislation was drafted, that we would be opening peoples' confidence in the markets?

Mr. HILLS. Really the act is almost two characters, two parts, and almost unrelated. We tried to seek control over internal books. There is a very broad point of view in the Commission that the Commission really didn't need that, that kind of internal control, but there are a number of people in the country that felt that the Commission did not have the authority to tighten the internal audit controls of the company, so we sought endorsement of that and super-imposed upon this is this thing called the Foreign Corrupt Practices Act, which put together is an illogical result, I think.

Mr. BLUM. Mr. Chairman, if I may, I disagree with Mr. Hills on the adequacy of no legislative approach, on the adequacy of disclosure through the IRS.

I am mindful of the fact that anything disclosed to the IRS can be disclosed to no one else.

Mr. HILLS. I am only seeking the private company.

Mr. BLUM. I feel very strongly that the kind of disclosure we are talking about is a disclosure by the company to the U.S. Government, which then creates a situation which forces the U.S. Govern-

ment to respond to that disclosure one way or another within a stated time.

That disclosure should involve amounts over a certain level so that the reporting requirements do not become burdensome. I believe that kind of disclosure will force the U.S. Government to become an actor in the situation and to recognize and deal with situations which are inimical to the national interest.

My objection to criminalization is not one that would be based on my believing that this is not a moral issue. Indeed, it is.

It is a very pragmatic objection, and the objection is I know from past experience, the Justice Department and I have now been in situations where I have talked to the Justice Department, where they are about to prosecute, they cannot bring those cases, ultimately every one of them would be stopped for the "national security problems."

There is nothing more silly than having law books which cannot be enforced.

Mr. WIRTH. Mr. Pollack, trying to step back to the period 1973 to 1977, what was the original thrust of the legislation? You and Mr. Hills were pointing out that disclosure was the key element. Do you feel that disclosure is adequate to meet the problem that we have?

Mr. POLLACK. I think that disclosure is a disciplinary or self-regulation device. If a company is required to keep books which are reasonably accurate, if a company is required to have internal controls which give reasonable assurance that they appropriately and adequately protect the assets and transactions of the corporation, you have not only the disclosure but you have the discipline, which also is exercised by the audit committees that Chairman Hills referred to. We now have in the security laws for broker dealers a requirement that they must keep very detailed records, and they must be truthful and honest, and that has been extremely helpful in surveilling the broker dealer community.

The Commission has the additional inspection power because of the regulatory authority that it exercises. The importance of the accounting provisions is that Congress gave a basic message to corporate officials that they would be held accountable for proper management of the corporation.

Mr. WIRTH. The SEC wanted to do that to start with.

You felt you needed congressional sanction for those steps; is that correct?

Mr. POLLACK. We thought we had some power to deal with it but we wanted to insure against attacks; let me back up a second.

When we were first investigating, we were charged with attempting to destroy free enterprise and with acting outside of our jurisdiction. That lingered on as this thing proceeded.

To partly offset that, and to partly also give the Commission the support of the legislative body to whom it is ultimately responsible, even as an independent agency—

Mr. WIRTH. We try to remind Mr. Shad of that.

Mr. POLLACK [continuing]. That this legislation would be very helpful. The two provisions that were adopted were part of the core of the Commission's thinking, and the Commission adopted a separate rule which makes it a violation for corporation officers and di-

rectors to lie to auditors, in an effort to strengthen the application of the legislation, and also has a provision that makes it unlawful for any person to falsify books and records of issuers required to report under the Securities Exchange Act of 1934.

That as a whole from the Commission's point of view was needed to overcome in a remedial way what had been uncovered because, as Chairman Hills has described, you had conduct that went all the way from gross illegality to what I would call questionable application of corporate funds.

Mr. WIRTH. Am I understanding the panel to say that you are all in agreement that the basic disclosure and accounting provisions are the fundamental foundation of actions that this Government should continue to be taking?

Mr. HILLS. If I may say this as carefully as I can, that is the foundation of the successful effort against the problem that was uncovered in the middle 1970's. That is the foundation of the success.

Mr. WIRTH. You all agree with that?

The dangling issue that Mr. Blum raised in an exchange with Mr. Hills related to privately held corporations. How does disclosure then come about to assure that privately held corporations conform with the regulations of the SEC as supported by the legislative language?

Mr. HILLS. All I meant to suggest was that a disclosure system comparable to that management by the SEC could be built upon the IRS, to give the same kind of public reporting to the Government for the kinds of commission payments, not just foreign payments, but the kind of commission payment that could be the basis of questionable conduct.

In other words, a different form of governance has to be contrived for a company that does not have the corporate accountability built into the public securities laws.

Mr. WIRTH. Mr. Blum?

Mr. BLUM. I didn't mean to misunderstand you. That helps considerably.

Mr. WIRTH. The statement that Mr. Hills just made clears up that misunderstanding.

Mr. Clinard?

Mr. CLINARD. I quite agree with what has been said. The heart of the control problem is disclosure and accountability.

Mr. WIRTH. We are trying to figure out how we got to here.

Mr. CLINARD. If I may ask a question of the panel, who have been with the SEC. Only something like three cases were brought during 4 years in violation of this act, that is, substantive cases, and about six, I believe, on the accounting part of it. Granted, that Stanley Sporkin was in the SEC in those days, it still is incredible to me, considering the history of foreign bribery, the evasiveness of it, and the sordid picture of it, that we only turn up, I think, three substantive cases and six on the accounting part.

Did not the SEC pay much attention to this act after it was passed? How come we don't have more than that? It is unbelievable that there are so few.

Mr. RINALDO. Will the Chairman yield for a moment?

The Chairman was on a very good line of questioning. I would like to go back to Mr. Hills to clear up one point.

We were talking about the accounting provisions. Before we leave that point, from your testimony I gathered you feel they should be changed but I am not certain as to how you feel they should be changed.

Mr. HILLS. I would be happy to give the Congressman the testimony I have given in the Senate on the subject of proposed changes. My principal feeling is that the heavy hand of criminalization has caused most of the problems with the existing accounting rules.

Mr. WIRTH. Is the heavy hand of criminalization like the heavy hand of Government?

Mr. HILLS. Let me give you an example. I am chairman of an audit committee, and we sit down once a year and look at 87 locations for an international company and the outside auditors come in with the inside auditors, and they hand you a big chart with circles and squares and that chart tells you the degree to which each of those locations will be audited.

Anyone, no matter how experienced, really does not know whether you ought to have a hand count inventory every third or second year at each of those places, but your job is to keep adequate internal controls; and if you don't you are subject to criminal penalties. It is so likely that the only place you didn't uncover fraud is the place where we didn't require an audit this year.

Are controls adequate? We are not afraid of the judgment of the peers in the business world or the lawyers or the accountants, but I wouldn't like that judgment submitted to a grand jury proceeding to determine whether I was prudent.

Having said that, I recognize both John Shad and Senator Chafee and you have been working with the proposed changes in the accounting provisions to adjust them to meet some of the legitimate objections of the accounting profession.

It would be a lot easier to reach that balance if it weren't for this criminal thing hanging over one's head.

Mr. RINALDO. You feel the criminal penalties in the accounting provision should be eliminated?

Mr. HILLS. To tie the two together, that cord should be broken.

Mr. BLUM. I would agree that they should be eliminated for non-willful violations, but where I think there is a deliberate attempt to deceive, then the criminal provisions should be there, and I believe they would be there under the Securities Act as they are now.

Mr. HILLS. Any time a material mistake or willful violation of the securities laws is made we have the basis under the securities law, to tie it to the Foreign Corrupt Practices Act, and agents overseas and dealing with foreign officials has put a color to it that is very difficult for people to deal with.

Mr. WIRTH. Let's make sure we understand. What you are suggesting is that criminalization for the accounting provisions of the act is not necessary and that the SEC already has that authority under section 32 of the Securities Act.

Mr. HILLS. Department of Justice has that authority.

What I am saying if you leave out entirely the whole subject of whether it is a crime to bribe somebody—

Mr. WIRTH. Leaving that whole side of the act aside for a moment, we are still discussing the recommendations made by the SEC and affirmed by the Congress regarding the accounting provisions of the act.

Mr. HILLS. That wasn't the subject for today's hearing and so I can't be as articulate as I would like to be. Yes, I do think there is room for modification of those provisions, but the principal problem as I see it is the linkage to this concept that it is illegal to make certain kinds of payments.

It is that connection that has caused in my experience most of the problems with the enforcement of the act. In most audit procedures, the problem really is with the smaller companies.

If you take a company that has sales of \$2 or \$3 billion and has dealt with this in a sophisticated fashion a long time, they have a sense of what can and cannot be done.

A small company that has not done business abroad has a great deal of difficulty adjusting itself to the accounting rules. Again, this was not the subject of this hearing so I can't be more precise than to say I do think the internal accounting controls could stand some tinkering with but I don't think it requires a major change.

The differences between Senator Chafee and Mr. Shad weren't that great.

Mr. BLUM. I can go back to Treasury where those accounting provisions came from in part. It was a rather memorable hearing which Exxon came to the Foreign Relations Committee to explain the payment of \$50 million worth of bribes in Italy through an Italian oil trade association.

The comptroller of Exxon said in the hearing room and was asked by the members of the committee straight away how it was that Exxon couldn't know at headquarters the \$50 million bribe was paid.

He said, "Senator, when you have a cash flow as large as ours, it is simply not possible to keep track of a sum as small as \$50 million."

This was breath-taking. In some sense I could sympathize and I personally investigated the episode and believed that the top management at Exxon did not know and was appalled and later tried to recover the money and couldn't.

The response at the time was to say, well, then, we will make sure you find out about those things and the way to do it is impose some kind of criminal sanction if you don't.

I don't know when you get to a corporation of that size, it makes any sense at all because, as Mr. Hills points out, it is very hard for an outside director to keep track of branches in 80 countries.

Mr. RINALDO. I would like to request unanimous consent that the record remain open so that Mr. Hills can submit his specific recommendations for changing the accounting procedure provisions so the subcommittee can consider them when we look at any changes in the act and for any additional information any other members of the panel would like to submit.

Mr. WIRTH. That would be very helpful to have recommendations from all of you.

I point out the purpose of this hearing was to try to get a sense of where this act came from and why.

We are taking the next leap, as long as we have all this good talent here.

Mr. HILLS. The committee might find it helpful, either in hearings or staff interviews, to have a series of individuals who serve as outside, independent chairmen of the audit committees of some of the large multinational companies. It might be useful to sit in on a meeting, an outside meeting with the outside audit committee and auditors.

Walking through that procedure would give a much better, I guess people call it hands-on feel on what is and is not a problem. It is there where the act is at its challenge. When the outside auditors and outside counsel and outside auditors meet outside the presence of the management of the company to try to deal with the financial accounting of the firm, I am sure it could be arranged to have the staff interview any number of people that are in that capacity, and then the committee might from those interviews decide to interview some of the people that serve in that role.

Mr. WIRTH. We will get back to that.

Mr. Clinard?

Mr. CLINARD. I would say that an examination of those internal audit reports indicates such extremely willful, diverse and clever things that I found myself extremely shocked. I think that that criminal provision should be applied to them. If I understand the comment correctly these were no open payments.

In the case of the Prime Minister of Japan, it was in cash. It was by diverse methods, and the willfulness of it is horrendously clear.

The corporate structure is such that if a director, chief executive, or president of a large corporation does not himself have access to exactly what is going on, then the corporation has the responsibility to appoint persons in terms of internal intelligence to find out what is going on. So I myself would hold to the criminal penalty on this type of thing.

I might say, having worked in this area for some time, that there is nothing corporate officials fear more than the criminal penalty. Corporate fines, and individual fines mean very little to the individual. Even if it is only a 2-day sentence in jail, a corporate executive fears that more than any other penalty you can impose.

So if you are going to have a deterrent, the criminal penalty must be preserved. There has been a lack of knowledge in top corporate circles as to what was going on, not that the bribe was made but how it was concealed.

Mr. WIRTH. Let me make sure I understand what Mr. Hills was saying.

I am getting confused as to what is being suggested.

Are you saying that section 32 of the Securities Act, that which provides criminal penalties for violations of the Securities Act, should not apply to the internal accounting controls provision of the Foreign Practices Act?

Are you saying that an exception should be made?

Mr. HILLS. My first premise, is that I think that the criminalization of conduct abroad has caused the problem. In other words, the characterization of a payment as a crime as distinguished from simply making sure the internal controls of the company expose it.

Mr. WIRTH. Leave the bribery aside.

Mr. HILLS. I understand. The securities laws generally are subject to criminal penalties for willful and material violations of the act. I certainly think that any willful violation of the accounting provisions that exist or the regulations of the SEC or the disclosure requirements of the SEC should continue to be a crime.

There has been some problem with it, because the word "material" has been missing, and that needs some tinkering with, but I wasn't suggesting for a moment that the criminal enforcement of material, willful violations of the Securities Act should be changed.

Mr. WIRTH. I didn't think so but I wanted to make sure.

I wanted to make sure we are not talking about any exception for the accounting provisions of the Foreign Corrupt Practices Act or any change in the application of section 32.

Mr. POLLACK. I have had some practical experience in enforcement in the criminal sector during my career at the Commission, and as I mentioned, we have broker-dealer provisions which require the keeping of honest books and records and as Chairman Hills has indicated, they are rarely used for criminal prosecution and then only for egregious cases. You can't prosecute somebody criminally for an inadvertent error.

You would be laughed out of court. You have to place this all in context. To bring a criminal prosecution for a violation of the accounting provisions, you would have to have very mischievous conduct which would hit the stomach of a jury, so that they would feel it was culpable enough, that they would bring back a verdict against the defendants.

And I think that should not be overlooked, that it becomes even more difficult when you talk about the bribery provisions because right in the act it has the term "corrupt," which is essential in determining what you must show and corruption has a well-defined meaning in the law in the corruption of witnesses and other places in the law.

So from the criminal point of view I can understand a board of laymen being very concerned because they are not as exposed as some of us who have been engaged in prosecution work, that it is very difficult to convict somebody in a criminal court as distinguished from maybe a civil action, and I just put that out to alleviate any concerns that may exist in the corporate community, that people will be hung by a grand jury and then convicted for miscalculations or negligence or something along that line.

I point it out because I do think there is an express concern of people perhaps based on a misconception on the protections that substantively and procedurally exist before something can be criminally prosecuted. I am not attempting to deny the facts Mr. Hills has referred to. People do get concerned when they see a criminal statute.

Mr. RINALDO. Do you agree with Mr. Hills, though?

Mr. POLLACK. I must say to you as an old prosecutor, I don't find those provisions from a criminal point of view ambiguous for a defendant. If they were, he could move to dismiss the charge on the ground they were vague and indefinite and, therefore a violation of due process.

I think reasonable is a term that is used in many statutes, and those provisions which were carefully reviewed when we were at

the Commission follow the accounting literature. They are well-entrenched in the accounting literature as to what should be done.

When you add, as was mentioned, that section 32(A) requires a willful act, you don't go to jail for something that is not knowing. You already have the protections against criminal prosecution. I am not saying corporate people don't get concerned when they talk to lawyers and accountants, because they do get worried.

Lawyers and accountants perhaps give advice that tends to worry corporate officials. Those who are honest are going to be more worried than somebody who is a schemer, but that is the balance that you try to reach. Those provisions do have a salutary, self-disciplinary effect, but in my experience over many years if you honestly conduct yourself, there is little if any chance of any honest businessman under these provisions of running afoul of the criminal provisions.

Mr. RINALDO. Your answer still supports the contention that Mr. Hills made. In effect, you are saying that you can understand why corporate officials would be inhibited as a result of—

Mr. POLLACK. I didn't say they would be inhibited but concerned. If an accountant says to you that you can go to jail and he does not really tell you that that is not really the fact but that is a theory, you may be concerned as a layman. I am trying to tell you as a professional, if I were an independent member of the board and I had to live with those provisions, I would not be concerned about criminal prosecution.

Mr. RINALDO. You also added that if the person is criminally prosecuted that you could move for dismissal. I don't think any corporate official wants to go through that even.

Mr. POLLACK. I don't think I was giving you that as a legal proposition applicable here. If somebody could argue that this was so vague that it was not within the due process provisions, he could move to dismiss it. Any lawyer will tell you it is a clear enough standard to permit criminal prosecution provided you show criminal intent.

You don't prosecute somebody without criminal intent under these provisions.

The only point I am making is that people get concerned about provisions when they add criminal penalties to it. It is an axiom. I do not personally find those provisions to be so vague that a reasonably honest person could not comply with them, and I think that the administration of the act shows that.

We have had reference to the small number of cases brought even civilly by the Commission. They have not brought that many in an effort to maintain the basic purpose of this act, which is to be remedial and not to engage in punitive actions.

Mr. RINALDO. I would like Mr. Hills to comment on your response to my question.

Mr. HILLS. We are both commenting in a vacuum in a sense. My comments have been on the assumption we did not have the bribery provisions of the Act and apart from that I can't deal with it.

It is difficult to sit as the chairman of an audit committee with, say, 80,000 employees all around the world, wondering what kind of discretion you can give them to do business and wondering what

kind of accounting provisions you must have to keep track of how they conduct their business.

I would assert again, we don't have it for this hearing, but I would assert that the combination of the bribery provisions and the tough accounting provisions under a criminal statute has impeded unnecessarily the doing of business abroad.

There are whole areas of the world where some major companies have chosen not to do business simply because it isn't practical to try to manage your personnel abroad.

It is not practical to engage in the kind of surveillance. Many places the only way one can do business is with a joint venture with another company with which you have to have a minority interest, and even there you are concerned about what kind of surveillance you should have over your partner not for the purpose of bribing, but simply because you cannot maintain the kind of controls that seem to be required by the statute.

We are not talking about condoning bribery or a wholesale reformation of the act, but we should recognize that the things that were uncovered by the SEC in the midseventies in my judgment were properly and fully addressed by the actions taken by the Stock Exchange, the auditing profession, and by the accounting provisions of the act.

With some modest changes in the accounting provisions of the act and substantial change in the criminalization part, not unlike Mr. Blum suggested, I believe we would have answered the legitimate concerns of the business people of the world and not at all impaired our capacity to stop the kind of mischief that we saw in the midseventies.

Mr. RINALDO. What you are really saying is you are going back to your description of the entire changes in the corporate governance and structures that have taken place in the past few years, and you feel those changes are going to be permanent?

Mr. HILLS. Absolutely.

Mr. RINALDO. Therefore, the act should be amended. Perhaps maybe it was good that we wrote it the way we did originally, because perhaps those improvements in corporate governance would not have taken place and at least now I assume it is our feeling that they will continue in place if the Foreign Corrupt Practices Act is amended?

Mr. HILLS. There is an impetus of change well underway. It has gone a long, long way. I don't suggest that all good will come out of this and all evil be eliminated, but the impetus of change is sufficient for the time being.

We could relax the criminal provisions, maintain strong accounting provisions, strong internal controls without impairing the business system that we have.

Mr. RINALDO. I am impressed by the fact that at this hearing, most of the witnesses, at least have indicated that the act does need revision, and that there are certain things that should be made, and I would like to on that basis go back to Ambassador Akins, if I may.

You indicated in your testimony, on page 4, that facilitating payments or "grease" payments as they are called, are common in many countries and probably necessary to do business.

Now, when I say that, I am referring to small payments to low level officials to speed up the performance of their official duties.

Could you indicate for the record from your experience in the Middle East and elsewhere how prevalent such payments are and how necessary they are to the conduct of the business and how they should be treated in the Foreign Corrupt Practices Act in your opinion?

Mr. AKINS. It probably is necessary, regrettable but necessary. In many countries, particularly poorer developing countries where officials are paid \$30 or \$40 a month, considerably below the living wage, they can make sure that your Customs declaration is not processed or that it goes to the bottom of the pile. You could have a delay for several months before it gets to the top.

It facilitates business to be able to pay an official a certain amount of money to get priority treatment. Nobody likes to do that. But to say that this cannot be done says that the company cannot do business efficiently in the country where he is operating. We might like to change the whole internal structure of a specific country and we will not be able to accomplish that.

It is difficult to define how much all minimal payments "is" \$10, \$15, \$20, or \$30, I would consider minimal. Several thousand dollars is not minimal.

Mr. RINALDO. Do you feel—

Mr. WIRTH. If the gentleman would yield for a minute to make sure we clarify that. We are not talking about wholesale reform of foreign governments.

In title I the definition of the term "foreign official" states "any officer or employee of a foreign government or any department, agency, or instrumentality thereof, or any person acting in an official capacity for or on behalf of such government or department, agency, or instrumentality."

In other words, somebody acting on behalf of the government. "Such term does not include"—and this is the "grease" payment provision for such things as unloading cargo on the dock "any employee of a foreign government or any department, agency, or instrumentality thereof whose duties are essentially ministerial or clerical."

Is that a definition that solves the problem you are talking about?

Mr. AKINS. As far as I am concerned it does. As far as a number of the companies I have talked to, it wouldn't clear it up.

The large companies who operated abroad for a long time generally, the companies who have 80,000 employees abroad, for example, know very well how to adjust to the problem.

The demand for clarification of the act I think, comes largely from the smaller companies and the companies that are just starting to go into business abroad.

I think you will get a lot more testimony on this. I have heard companies claim they have not gone abroad because they are not exactly sure what the criminal penalties under the act if they are operating in a foreign country.

They know they have to pay the harbor master something. Is he a high official or isn't he? They don't know. And they say they do not take chances; hence they do no business.

Mr. WIRTH. Any other comments on that?

Mr. BLUM. I think there is a concept that might be well worth considering. That is where should the United States legislate with respect to the conduct of its citizens and at what level does the national interest rise to the point where we try to control their actions overseas?

Normally if I travel overseas and violate the laws of a foreign country, I am subject to the criminal penalties of that foreign country.

I think that the only time the United States should properly involve itself in my activities in that foreign country where I commit the act is when I am doing something that is so inimical to the U.S. national interest that Congress feels it necessary to legislate.

The business of making a facilitating payment I don't think rises to that level. I think there is a serious question of jurisdiction. That is really a problem for the local government. To that end, the United States can do certain things. We can encourage local governments to clean up their act. We can renegotiate a wide range of treaties we have with those governments which will enable them to investigate criminal wrongdoing by any American in their country. We can become aware as a nation of a very rancid situation in their civil service and forcefully call it to their attention.

There are things which can be done.

Mr. RINALDO. Yes, but a government over there—I am sure you recognize our Government over the past several years has tried to reach an international antibribery agreement. They have been unsuccessful. Perhaps even the present law that we have on the books with its problems and ambiguities has been a handicap to reach that agreement because I could conceive of a situation where another nation would be reluctant to adopt a proposal which has caused so many difficulties for American companies.

Mr. BLUM. Well, let's back up here.

I am talking now not about an agreement among the developed countries, the OECD countries, each in turn to curb their own corporations' activities in third countries.

I am talking rather about those extradition and judicial assistance treaties the United States has with most countries around the world.

I am talking about helping those countries wherever they may be in enforcing their own laws. There is no country in the world that has laws that condone bribery as we have already pointed out.

Those treaties that we have are very weak. They were negotiated many years ago. They do not permit appropriate extradition. There are a variety of difficulties that those treaties have. They can be cleared up.

We have had that whole process of renegotiating these treaties on a back burner for many years. It is something that gets a very low priority on the list of State Department activity. It is something which I think should be speeded up and given a lot more attention.

I will give you some examples. Crimes, to be extraditable, have to be identical crimes in the two countries, both the requesting country and the country from which the person is being extradited.

In the last 20 years we have defined an entire new range of Federal crimes dependent on interstate transportation or interstate communication that are now not extraditable and not subject to judicial assistance.

Mr. WIRTH. Why don't we move to Mr. Collins and come back?

Mr. COLLINS. Thank you, Mr. Chairman.

I am very much concerned about what foreign practices are illegal. I think most businessmen, the great majority, try to do the right thing. It is just a smaller group that does not. One thing that always impresses me in Washington is that this is the most self-righteous city in the world. When we start passing all of the judgments, I wonder just what is the fair and accurate basis on which to do it?

In fact, in the Commerce Department, we issue a statement on oil imports which is very misleading.

As I understand it, if the oil comes through the Virgin Islands, we do not list that as an import.

That is about as much doubletalk as you could ever have, the fact that because it came through the Virgin Islands, it is not listed as imported.

The other thing that impresses me is our Federal budget.

When it comes to accounting, the last figures I saw, we had \$25 billion of what they call nonbudget items which we don't even show to the American people. We talk about how much the deficit is; yet we have these items go through the back door to the national debt.

I can't find where—our standards here in Washington—are a yardstick. No one ever pays a stewardess anything, but they tell me in some of these countries if you are going to ever get anything out of the Customs Office, a payment is considered part of the guy's salary.

In the United States that is not true; but in some countries they think that is part of their salary.

Would the Ambassador comment on the matter of actually expecting to be reimbursed if they give your shipment a priority to clear it through Customs?

Mr. AKINS. I don't think there is any doubt about it. Salaries are very low. They can't live on their salaries. This is known by the Government, but instead of raising salaries to a living wage—which it should do but probably doesn't have the resources to do it—says we will look the other way when the touch is put on the foreign companies operating in this port or on the visa offices or what have you.

But I think that we have all agreed that we are not talking about this law level corruption.

My only reason for raising it in my written testimony and here is that there seems to be an ambiguity on this matter; there are companies operating abroad which believe the act does apply to this type of payment. If this can be cleared up through a new interpretation of the act that would be fine. If not, then perhaps there will have to be a change in the act.

I don't think the FPCA really can apply to these minimal amounts.

If it does, what we are saying to all countries in the world, is that they should give all of their employees living wages. Fine. Jack Blum might like to negotiate treaties with the countries of South Asia to do this, but it would be very difficult.

Mr. COLLINS. Let me go into another situation that comes to mind. I don't quite understand where this matter of bribery comes in.

I know of a case where a general represented a company in a foreign capital. He was providing legal services as he construed it. He had been the campaign manager for the President. Whatever they paid him kept them from waiting—they hadn't done anything wrong, but just to exist in the country you had to have this fellow process your papers.

Is paying that general for that legal service dishonest under the present law? That guy is no more a lawyer than anything, but he is the only one that can make the paper move in that country. This is an actual case.

Mr. AKINS. I think that probably it is illegal under the act. The lawyers will have to answer that.

My suggestion was on the use of agents abroad. If payments made to this general is known, is published or otherwise disclosed, and the government involved does not object, then I suppose I would not object to it either. But I also suggest that every government in the world, no matter how backward, or how basically corrupt, will not be able to tolerate corruption without risking internal dissent. Revolution against the governments which allow huge payments to government officials is scarcely unknown.

This gets back to what we—all of us—talked about; the necessity of disclosure.

Mr. COLLINS. Let me ask one thing. I am not quite sure. Do we record all of the fees paid to lawyers in Washington? We don't record those fees at all?

Mr. POLLACK. No. Only for lobbyists.

Mr. COLLINS. Only the lobbyists?

Mr. HILLS. Only reimbursement for time spent dealing with the Congress or in lobbying for a bill.

Mr. COLLINS. We all know in Washington that some lawyers have more access than other lawyers, and access is one of the most valuable things you can have. Is access in any way a form of indirect—I don't want to use the term bribery—but indirect influence?

Mr. HILLS. That is a question that no one wants to answer, Mr. Collins. I am sure it is true that it may be perceived at least by the seeker of services that some have more influence than others; whether or not the people who are sought hold themselves out as having "influence" is a different issue.

Certainly as you look at us, and look at others, you see some similarities in terms of what you pay for. We who go to a foreign country want to know somebody, not necessarily who has access, but certainly someone who is able to predict the outcome of something that you may wish.

If you are seeking a joint venture in a country that is entirely socialistic, entirely owned by the government, you surely want to find someone who has access to the government in order to promote your joint venture.

There are some very conservative countries where almost all the means of production are owned by the government; not just the socialistic countries behind the Iron Curtain.

To do business in those countries, and to pay facilitators, lawyers, accountants, business people, agency fees, I think that like Will Rogers said, every story is either too little or too big; nothing is easily defined. But surely in many situations, in a construction firm, for example, they may not wish to have a business operation in a country where the government owns all the business because the agency fees alone would look like a bribe.

The typical agency fee on a \$700 million refinery is a very large fee and it is mind-boggling to decide whether that would be a violation of the Foreign Corrupt Practices Act or not, particularly because in many of the smaller countries the elite class, if you will, the educated class, tends to be from large families.

Some of the most distinguished people in the world have their brothers as prime minister. Some of the most honest people in the world have fortunate circumstances where their family members are in high government offices.

Mr. CLINARD. It seems to me that it is very difficult sometimes to define a bribe. A bribe is something, either money or some other thing, that perverts the conduct of a person in a position of trust. That is entirely different from influence or contact. That is, it perverts his conduct. He is in the position of trust like a high official.

About the problem of customs officials, I have a suggestion on that, having lived abroad a lot, having paid money to get my own things through customs. For a customs official to violate the law of his own country, and we conspire in that simply because it is a small amount, still is a difficult situation. I was thinking that a fixed limit should be set. It is very vague the way it is now, particularly for a small company that doesn't know how to operate.

If it were limited to say \$200, \$500, in actual monetary fee, as a maximum, that might clarify things a little bit.

Can you really corrupt a high official for \$200? I doubt it. That would enable people to distinguish more clearly a Customs fee and so on.

As I say, that raises a problem of acknowledging in our own law that we are violating the laws of another country. I go for a monetary limit on the amount.

Mr. HILLS. May I make this observation? Somebody once paraphrased that famous comment by Justice Potter Stewart when he said, "I can't define pornography, but I know it when I see it."

Someone before the Commission once said, "I can't define a bribe, but I will know it when I get it."

The issue that I think you should focus on as you amend the law is this: And I think Mr. Pollack would agree with me. In dealing with the problem that we perceived at the SEC, were the bribery provisions not passed—which is a different issue as Mr. Pollack said—had we merely been given the authority of the accounting provisions with its own criminal enforcement procedures, the problem that we perceived during the middle seventies in my judgment was dealt with.

To go forward and add the bribery provisions to try to criminalize conduct abroad and try to define between a good bribe and a

bad bribe and a grease payment, and so forth, I don't want to moralize.

All I want to say is from my experience at the Commission and from my experience in business, without those provisions we would be dealing completely with the problem we perceive in terms of questionable corporate payments.

That does not necessarily mean you don't want to have a bribery provision, if you understand what I am saying. It seems to me as you approach the bribery laws where you are trying to enforce a law, a criminal law against conduct in a foreign country, and you think it is important, you ought to approach it from the standpoint that it is not needed to deal with the problem uncovered by the SEC.

Mr. BLUM. Mr. Collins, I am struck by the fact that Congress, in its wisdom, passed some very extensive laws with respect to the question of access. I, for example, have to disclose my campaign contributions, political action committees disclose their campaign contributions. Disclosure is the device that the United States has used to deal with that question of preferred access.

Mr. COLLINS. I had a case come up in this country where a big factory at home opened an office in a city up north. The first year they took over their factory, the real estate appraisal was tripled. They said, what do we do? They were told they didn't have the right lawyer file it at city hall.

They hired a lawyer at a very high price. He carried it in. The next day it was reappraised.

Certainly everything they did was completely honest, but I think that was an unfair influence situation. We don't have that in Dallas. I will say that about my city. Everybody pays the same.

This is an actual case. He was terribly upset, but it didn't take him long to get straightened out on the system.

I don't see how we can ever eliminate the system of having good lawyers represent you because that is the only answer anywhere.

Mr. HILLS. Thank you for that.

Mr. COLLINS. Nor do I ever advocate that they file their fee schedule. That depends upon the work they do and the magnitude of it, but I think we get to a pretty fine line when we write a law like this as to what is access and what is an indirect substitute of funds.

Thank you, Mr. Chairman.

Mr. WIRTH. I would like to briefly go back, Ambassador Akins, to the initial exchange between you and Congressman Collins, where he was talking about "grease" money and the inevitability of it. That was the thrust of the Congressman's question. I would like to go back to the quote that I read from the existing public law and then get your reactions to see if there is any problem in the differentiation between the intent that we were talking about earlier with Mr. Hills and the "grease" money.

Is there any problem with the language that says such terms do not include any employee of a foreign government or any department, agency, or instrumentality thereof whose duties are essentially ministerial or clerical?

Do you see any problem with that part of the statute?

Mr. AKINS. I said earlier as far as I am concerned there is no problem. It is quite clear that does not apply.

Mr. WIRTH. I wanted Congressman Collins to hear that.

Mr. AKINS. I also said it is a problem, I know, for a number of companies who are operating abroad because they are not sure whether it applies to them.

Mr. RINALDO. Would you repeat that with the microphone a little closer?

Mr. AKINS. I said as far as I am concerned it is quite clear. I also said as far as a number of companies operating abroad, it is not explicit enough.

That is the only reason I think we are talking about changing the law, to make it more explicit; not to reduce the criminalization of acts of bribery.

I haven't addressed the question of criminal penalties. As far as the companies operating abroad are concerned, it is the imprecision in the act they complain about. They don't know whether they are going to be held liable for an action they think is legitimate.

Mr. RINALDO. You feel then it should be changed?

Mr. AKINS. I do.

Mr. WIRTH. I understand that.

What I am talking about is the distinction we are making here between the unloading at the dock. That is not the issue we are talking about and the act attempts to define that away in this language here that talks about who it is that is at issue, people representing the government or people effectively representing themselves.

Mr. HILLS. Mr. Chairman, just take the unloading at the dock, for example.

Let me give you two real examples. During the discomfiture in Iran, many ships were stuck in the harbor. Many ships got out by bribing the harbor master. Everyone would say you have \$1 million on your ship, protect the corporate property, the harbor master's act was ministerial, he should let them all out. Therefore you are exempted, no matter how many thousands of dollars you may have paid that harbor master to get out. It is ministerial? It could be several hundred thousand dollars.

Take another case. In many ports of the world today there are enormous backlogs of ships. You can look off of Newport News and see ships waiting to load up coal. You can go to Kuwait and see hundreds of ships waiting to unload supplies into Iraq because the Iraqi ports are closed by the war with Iran.

The captain that is standing out there at the end of the line—if he can get his ship unloaded first, ahead of some others, that may be worth millions of dollars to him. It is purely a ministerial act to decide which is the order of ship unloading, but with the restrictions on the harbor, a \$1 million bribe paid to the harbor master to let that ship in out of order—and for that matter these may not be any order—it is very difficult to say that is a ministerial act.

Another case in which you are getting customs through, you slip somebody \$5 because he is a good guy and he smiled at you, tip like you give a porter, or, as I say, if you get yourself taken out of order on a contract in which you are able to secure minerals contracts in large countries.

You may be giving it to a clerk, but you may be getting an enormous corporate benefit out of a ministerial act. I say it is beyond definition.

Mr. WIRTH. Mr. Ambassador, can you respond to that?

Mr. AKINS. I certainly would not like to have any figure placed on the amount that could be paid without suffering penalties. Certainly a \$500 maximum should not be mentioned.

You can sometimes get a visa or residence permit for \$20 but if Congress puts a \$500 limit, it suddenly becomes the floor, not the ceiling. Why pay \$500 for something you can get for \$20?

We are repeating ourselves now. It gets back to disclosure. If you are paying \$1 million to get a ship jumped up in line and you disclose this to the American officials, it will be known in the country involved as well. If they know that this is being done, they will take action against the official who is doing it.

They won't take action against the customs official taking \$10. That is part of his salary. They will take action against the official taking \$1 million.

Mr. RINALDO. I think it is obvious, Mr. Chairman, from what both these gentlemen have said in response to your questions, that there is difficulty with the language that you quoted as currently written and that we will have better examples before us, I am sure, when we hear from the companies involved on the problems that they are experiencing not only with that language, but with the act itself.

Hopefully at that time we will be able to get a better handle on it.

Mr. CLINARD. One of the things that bothers me in the discussion we have been having is one I would like to return to. That is why there has only been, I believe, some three substantive prosecutions—I believe I am correct.

I don't know how far they went, and only six under the auditing. Does this mean that—to me that means the act is very effective.

I don't know whether it means perhaps the enforcement has been not carried out on this particular act or it may mean they are more clever.

I don't know whether people here at the panel can comment on that.

Mr. AKINS. I would like to add something to that point too. I have raised this with the companies who brought the subject up with me over the last few years.

The fact that very few—there have been very few prosecutions, almost none. In those cases it was fairly flagrant examples of actions by the companies. I've asked them if they really say they are being honest and really are not breaking the intent of the law, why worry about the wording?

They say, "Well, that is quite true. We know there have not been very many cases brought against companies, but we are afraid of it nonetheless." That presumably is why we are considering amending the law.

Mr. WIRTH. Let me ask you then, as Mr. Hills pointed out, I think, in a very convincing fashion, a question regarding the ambiguity in the existing language between what is representing a gov-

ernment and what is representing yourself. You can use that as a summary.

Let me read you the other, proposed language. Subsection (a):

"Shall not apply to any facilitating or expediting payment to a foreign official which is customary in the country where made and the purpose of which is to facilitate or expedite performance by such official in his official duties."

Does that clarify better what existed before? It may be difficult for you to respond, having just heard the language by my reading it to you.

Mr. HILLS. If you take my ship cases, I think it is very difficult to say whether that is a facilitating payment. It is customary—

Mr. WIRTH. Seems to me you are right in the same box you described earlier.

Mr. HILLS. If I have to do it, it better be customary. The issue is whether the conduct I am engaging in is an appropriate thing for a corporate officer in light of his responsibilities to shareholders, to his sense of morality, and to the good will of the country abroad.

If I have a very large amount of money held up arbitrarily and the only way I can get that out, and if I feel that the thing I am asking to be done is moral, is responsible, and is my responsibility as a corporate official, I really do not want to conduct a poll to find out whether it is customary.

Mr. WIRTH. It seems to me this is even more ambiguous, to say "which is customary" in the the first part.

The second part is "the purpose of which is to expedite or facilitate performance by such official of his official duties," the purpose of which is to bribe him.

"The purpose of which is to facilitate or expedite a performance." What does this mean?

Mr. HILLS. The real world doesn't work that way.

In many cases where somebody is engaged in irregular conduct, a substantial corporation in my judgment just will not do business there. They don't like it. They are not going to go into a port where they have to spend \$5,000 or \$6,000 to get their cars in and out. They won't do business here.

Where they are faced with it using the State Department, often using the foreign office in a foreign country, you can deal with it.

The real world gives you unusual circumstances. You are faced with a decision you may have to make in 20 or 30 minutes. You may have a human life involved. You may have a threat to a household involved. Those are the real life problems that are faced that can't easily be dealt with by rigid criminal law.

Mr. WIRTH. It seems to me we have some very severe definitional problems there.

Mr. HILLS. Mr. Pollack and I were just chatting. Let me try once more to say what I think. A very serious problem was uncovered in the seventies. The various bills before Congress now are approaching two parts of it.

One, they are looking at the accounting provisions.

Second, they are looking at the criminal provisions.

I think all of us who suffered through the period in the SEC would gladly give up all the criminal provisions if you would leave the accounting integrity basically alone.

I don't mean to say there can't be changes in it, but we can effect the system of corporate responsibility that we have if the kinds of accounting, the accounting integrity, the books and records integrity that was accomplished by the enforcement division, which I might say was begun by Mr. Pollack, and by the SEC, if the entire criminalization of bribery was thrown out of the act, we can still deal with the integrity accomplished by the SEC's work.

Mr. WIRTH. Let me close by asking Mr. Akins and Mr. Blum to respond to that, going back to your opening comments.

Mr. Ambassador, you cited earlier a discussion in which you were told that we should be proud to have this legislation on the books.

Mr. Blum, you were talking about the impact this legislation or changes in this legislation might have on the perception of U.S. foreign policy, the fundamental purpose of the legislation being to enhance our foreign relations.

What do you two react to the suggestion that Mr. Hills just made?

Mr. AKINS. As to decriminalization of the act?

Mr. WIRTH. Do you want to quickly summarize that again?

Mr. AKINS. No. I think Dr. Clinard answered that. Businessmen really fear the criminal penalties. If the criminal penalties are removed, then his fear, which I share to a certain extent, is that their current business practices which are really quite good might be changed if they don't have the fear of criminal penalties hanging over them.

Mr. BLUM. I think the problem is this: The criminal penalties—and this goes to something Dr. Clinard said—are not enforceable.

I want something that will work. I believe the reason for so few prosecutions, inasmuch as I have been contacted with great frequency by the Justice Department, is what I encountered in my own past experience as an investigator. I believe many of the prosecutions have simply been dropped for foreign policy reasons.

We cannot be in the situation of indicting a U.S. corporation for bribing a high foreign official without causing a foreign policy catastrophe.

We have very strong national interests in preventing high level bribery. I submit that it is not simply whether or not the bribe is material to the corporation which is at issue.

There are some very clear and different kinds of standards which apply. We can tell pretty quickly when a bribe will undermine national security in the sense of giving away military secrets, exposing someone to blackmail, disrupting our relations with a foreign government, and in those conditions we have to be able to stop the act or at least create a set of circumstances where the act is so dangerous for the corporation it won't undertake it.

So some different kind of disclosure standard other than materiality to the corporation which would be the pure SEC approach, I think is what is at issue.

I think we can't just throw away the other portion of the act. I think the criminal approach to it is a mistake because, as I said, it simply is nonenforceable.

Mr. AKINS. Mr. Wirth, do you know of any such cases that have been dismissed because of foreign policy?

Mr. WIRTH. We are certainly going to ask the Justice Department about that as part of our staff investigation.

Mr. BLUM. I can't say with certainty. I have some beliefs. Because they were matters under investigation, I would rather not discuss them.

Mr. WIRTH. Do you know of any?

Mr. AKINS. I know of none.

Mr. WIRTH. Dr. Clinard.

Mr. CLINARD. I feel strongly—not for the bribery alone, but about all laws affecting corporations, that the criminal penalties is what they fear the most. I interviewed the chairmen of the boards, presidents, CEO's of a number of the Fortune 500, confidentially, without names, and there is no question that they feel that many corporate laws and regulations are to protect the honest, ethical, public-spirited corporation that is proud of its record from those that are unscrupulous. In my examination of reports to the SEC, and from the records I clipped from the Wall Street Journal and elsewhere many still did not engage in foreign bribery.

I think myself the criminal penalty is to protect the honest corporation that is trying to be ethical in its business conduct overseas from those that are not. Let me give you an example. IBM had practically no foreign payments.

In my 2-year study conducted with the cooperation of government agencies and other data, 40 percent of the U.S. giant corporations had not been charged with a single violation of the law by 25 Federal agencies during a 2-year period. On the other hand a small handful of corporations, Lockheed being one of them, Gulf another, have been charged time and again with violations of law.

So my own feeling is that these laws on bribery are not only for our image before the world, but they are to protect an honest business concern that is trying to preserve the tenets of capitalism from those that are dishonest, unethical, corrupt, lacking in social responsibility and so on. All of these top officials I talked to said fines mean nothing. The one thing they feared—this was unanimous were two things. One, they feared the criminal penalty. The second thing is a great deal of publicity. When I started my remarks, I said the publicity against American corporations, if that law were modified and opened up to bribery, would be, in my judgment, tremendous.

I want to make my strongest emphasis on those corporations that are trying to do good work. Pitney Bowes, IBM, I could name a whole host of them. They were not making payoffs. A lot of them were in it, but a lot of them were not.

That is what I think we have to think of in our decisions.

Corporations fear most the criminal penalties, whether subject to them or not.

The fact they fear them is somewhat of a deterrent. Whether they are used or not is immaterial. They don't know that.

Mr. WIRTH. Gentlemen, thank you very much.

Mr. Rinaldo, thank you. We greatly appreciate your lengthy attention to this this morning. It has been a long morning, but I think very useful to Mr. Rinaldo, Mr. Collins, me, and to the subcommittee record.

We will be meeting again on this issue within the next 3 weeks to hear from the Securities and Exchange Commission and the Justice Department, which will be followed by a third set, as Mr. Rinaldo pointed out, from affected companies and their perspective.

Thank you very much for being with us. We look forward to being able to work with all of you as we get into chapter and verse on this.

Thanks ever so much.

Mr. RINALDO. I want to join you, Mr. Chairman, in thanking the witnesses. I thought they were very good. They gave us a better idea of the problems associated with the act and the types of provisions that are needed.

Thank you.

Mr. WIRTH. The committee will be adjourned.

[Whereupon, at 12:05 p.m., the subcommittee was adjourned.]

FOREIGN CORRUPT PRACTICES ACT— OVERSIGHT

WEDNESDAY, NOVEMBER 18, 1981

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON TELECOMMUNICATIONS,
CONSUMER PROTECTION, AND FINANCE,
COMMITTEE ON ENERGY AND COMMERCE,
Washington, D.C.

The subcommittee met, pursuant to notice, at 9:40 a.m., in room 2332, Rayburn House Office Building, Hon. Timothy E. Wirth (chairman) presiding.

Mr. WIRTH. Mr. Chairman, welcome. Mr. Fedders, thank you very much for being with us.

Today the subcommittee resumes its oversight hearings on the Foreign Corrupt Practices Act. I think before we get to our first witnesses this morning it would be useful once again to set out why we are here and what it is that the subcommittee is doing in these hearings.

The Foreign Corrupt Practices Act was passed in response to disclosures of foreign bribes, illegal domestic political contributions, commercial bribery, and other activities which flowed from the slush funds, secret bank accounts, and corporate accounting practices, which reflected on the entire character of corporate management's stewardship over assets belonging to public shareholders. These practices seriously affected our foreign policy and national security interests in many countries and undermined public confidence in American business at home and around the world.

This administration now wants to change the act. It is said that the act has hampered U.S. companies doing business abroad and has destroyed America's competitive edge in foreign trade. There have been several legislative proposals which seek changes in the act.

Last spring the subcommittee was approached by a number of groups who told us the bill introduced by the gentleman from New Jersey, Mr. Rinaldo, was the answer to all the problems in the act. We were urged to pass it with dispatch. The same bill was introduced by Mr. Chafee in the Senate.

Now we understand that the latest version has undergone substantial changes before it emerged from the Senate Banking Committee. There are still open items which the committee could not resolve. These items apparently have been saved for consideration on the floor of the Senate, which is going to happen apparently within the next couple of weeks.

I was not sure that the legislative proposals I saw were the answer to any problems in the Foreign Corrupt Practices Act, if indeed there were problems. But I was willing to approach this issue with an open mind.

So we undertook to do a careful review of the act. In our first hearing we reviewed the very foundations of the law. We looked at the public policy considerations underlying the act to see if they have continuing validity.

Our next step, which I believe is a logical one, is to look at how the act has been enforced. We should know if there have been prosecutorial abuses. Another very important consideration, and a necessary one, is to consider whether the agencies have been doing their job in carrying out congressional intent under the act. We need to know whether the widespread abuses which gave rise to the act are continuing today.

We have received a great deal of information from the SEC and the Department of Justice. We appreciate that and are assimilating your good information.

After this hearing there is another important step. If indeed the act has been an impediment to legitimate business activities, we should find that out. On October 5 we sent letters to Ambassador Brock, the Special Trade Representative, and to the Departments of State and Commerce, asking for detailed information on the actual impact of the Foreign Corrupt Practices Act on exports and on foreign trade.

We asked that they supply us with information by November 1. Some representatives of these agencies have strenuously argued that the act has serious detrimental effects on American business and foreign trade. They should be the experts and they should be able to document those allegations. Yet it is now November 18 and we still have not received a response from the Special Trade Representative, from State, or from Commerce.

When we do, our next step is to schedule hearings to carefully review the data which they supply. In other words, let us look at the allegations and see what the data says and go from there.

Finally, some members of the business community have requested to submit statements and testify about their experiences with the act, and we will consequently have a fourth day of hearings involving those groups.

That is where we are going. We have laid out that course before. I thought it would be useful to do so again. Let me close by stating to all of those who are interested in changing this act that we will not legislate on assumptions, on undocumented surveys or on anecdotal evidence. There are important public policy considerations at stake. We will gather the evidence and data we believe necessary in order to act responsibly. Then and only then should we consider changes in this important law.

Mr. Collins, do you have a statement before we get going?

Mr. COLLINS. Thank you, Mr. Chairman.

I am pleased that we are now moving forward with the hearings to consider the Foreign Corrupt Practices Act. I look forward especially to hearing from our witnesses today who are going to discuss the enforcement of the act. I would particularly like to welcome Chairman John Shad from the Securities and Exchange Commis-

sion. Mr. Chairman, it is always a pleasure to have you, and I think your testimony today will be most beneficial for our committee.

I want to hear about the problems which the Foreign Corrupt Practices Act has caused for American companies. I have heard from Bill Brock and from some others who are keenly concerned about increasing our exports. The act and its ambiguities have exercised a significant limitation on U.S. export ability.

I hope you will share with us today your views on how it can be improved and how the act can be clarified to lessen these unnecessary burdens on American business.

Mr. WIRTH. Mr. Rinaldo.

Mr. RINALDO. Thank you, Mr. Chairman.

I was pleased to hear your statement. I hope that we move along expeditiously with these hearings, because I certainly think it is important that we proceed with any possible changes in the Foreign Corrupt Practices Act.

I look forward today to the testimony of Chairman Shad on enforcement of the act and would like to have, and hope we have, a discussion of improvements that are necessary in the act's operation. I welcome and encourage, in fact, the comments and recommendations of the witnesses this morning.

As you know, I introduced H.R. 2530 last March. I continue to feel very strongly that changes in the present law are necessary to remove serious impediments to American exports without weakening any of the prohibitions against bribery.

I also wish, Mr. Chairman, to emphasize, as I have to you in the past, that I am not locked into this bill as now written, and I hope the witnesses understand that, because I feel that certainly it is incumbent upon us to come up with the best possible piece of legislation. And I would be happy to consider any amendments or any other proposals that would remove the impediments that are currently existing and that we have heard about without permitting bribery.

Thank you.

Mr. WIRTH. Thank you, Mr. Rinaldo.

And as I noted in my opening statement, the question of serious impediments are raised again and again. What we are asking for and have asked Mr. Brock and others for are more than anecdotal evidence that this exists. What do we really know about this? Have there been serious impediments and has this really affected us, or are people assuming that there has been?

Let us take a look at that and get into the evidence, and that is what we are attempting to receive from the Commerce Department and from the State Department and from the Special Trade Representative. That is not the thrust of the hearing today. That is the next time through.

The hearing today focuses on enforcement. And again, Mr. Chairman, I am delighted that you are here.

Mr. Broyhill, do you have any comment?

Mr. BROYHILL. No; I just want to welcome the chairman and the members of his staff here today. We are delighted to have him here and to have his comments on this particular matter which we are all concerned about.

Mr. WIRTH. Before you get going, Mr. Shad, I also want to thank you for having Mr. Fedders' very successful visit to Denver. We heard a lot of good feedback from that. Thank you very much.

STATEMENT OF HON. JOHN S. R. SHAD, CHAIRMAN, SECURITIES AND EXCHANGE COMMISSION, ACCOMPANIED BY JOHN M. FEDDERS, DIRECTOR, DIVISION OF ENFORCEMENT; AND EDWARD F. GREENE, GENERAL COUNSEL

Mr. SHAD. Chairman Wirth, Congressmen Collins, Rinaldo, and Broyhill, the Securities and Exchange Commission appreciates this opportunity to testify on the Foreign Corrupt Practices Act of 1977.

With me at the table, as you have acknowledged, are John Fedders, the Director of Division of Enforcement, on my right; and Edward Greene on my left, who is the General Counsel of the Securities and Exchange Commission. These gentlemen have had considerably more experience than I have had with both the evolution and the administration of this act.

I will summarize the Commission's written testimony, which we previously submitted. It includes our testimony before the subcommittees of the Senate Banking, Housing, and Urban Affairs Committee with respect to S. 708, the Chafee bill, which would amend the Foreign Corrupt Practices Act.

The FCPA, as Chairman Wirth has amplified, was unanimously enacted in December 1977 in response to disclosures by more than 400 companies of questionable payments at home and abroad involving millions of dollars.

The Foreign Corrupt Practices Act accounting provisions require issuers to keep accurate books and records in reasonable detail and to maintain internal accounting controls sufficient to provide reasonable assurances, among other things, that transactions are executed in accordance with management's authorization and recorded as necessary to permit the preparation of financial statements in conformity with generally accepted accounting principles.

The SEC also administers the civil prohibition of bribery applicable to publicly owned corporations. All other companies or concerns are subject to civil and criminal bribery prohibitions administered by the Department of Justice.

Since enactment of the Foreign Corrupt Practices Act, the Commission has brought 16 enforcement actions. These include 13 injunctive actions to prevent future violations of the accounting provisions, one administrative proceeding involving the accounting provisions, and two injunctive actions to enforce the bribery prohibitions.

Each case has involved alleged violations of other provisions of the securities laws. The accounting cases have involved: Improper accounting with respect to questionable payments, exaggeration of sales and assets, failure to keep adequate records, misappropriation or diversion of corporate assets, and unauthorized management prerequisites.

The amounts involved have ranged from \$110,000 to \$23 million. Most of these cases have also included allegations that individual defendants aided and abetted violative conduct by the issuers—alle-

gations that are consistent with the Commission's position that inadvertent conduct will not give rise to enforcement actions.

Neither of the bribery cases involved accounting violations, but each included alleged disclosure violations. S. 708 proposes consolidation of the civil and criminal enforcement of the bribery provisions within the Department of Justice. In the Commission's testimony on S. 708, we did not object to such consolidation in the Justice Department.

The SEC recognizes that the Foreign Corrupt Practices Act has spawned unanticipated problems for American business abroad and uncertainties concerning compliance with the accounting provisions.

On January 29, 1981, of this year, the Commission issued a policy statement in response to concerns that compliance with the internal accounting control provisions has proven to be unduly costly and might result in liability for de minimis or inadvertent violations. The statement encouraged companies to develop innovative and cost-effective accounting systems and controls, to modify and improve them as circumstances change, and to correct recordkeeping errors without the chilling fear of penalties or the inference that past violations have occurred.

The statement pointed out that in each of the enforcement cases the Commission has brought under the accounting provisions, the requirements were breached as part of violations of other provisions of the Federal securities laws. It also declared that the principal purpose of the act is to reach knowing or reckless conduct, that inadvertent recordkeeping mistakes will not give rise to enforcement proceedings, and that an issuer need not always select the best or the most effective control measure as long as the one selected is reasonable under the circumstances.

Given the uncertainty that exists concerning compliance with the accounting provisions, the Commission has indicated that it would support amendments to clarify the law. The suggested revisions are principally intended to afford corporate management greater latitude and to reduce the uncertainties and burdens of the act.

Concerns have also been expressed that the bribery prohibitions have impeded legitimate foreign trade. On February 21, 1980, the Commission requested public comment concerning these prohibitions. The response was too limited to permit a fair assessment of the concerns, but the Commission issued a policy statement that it would take no bribery enforcement actions with respect to transactions cleared under the Justice Department's Foreign Corrupt Practices Act review procedure.

The Commission has also provided interpretive guidance on the accounting provisions through two rulemaking proceedings. The first, in February 1979, prohibited falsification of corporate books and records and false or misleading statements to accountants in connection with audits or examinations of issuers' financial statements.

The second, in April 1979, proposed inclusion of management reports on internal accounting controls in annual 10-K reports. This proposal was withdrawn in June 1980 because of concern raised by over 90 percent of the 950 commentators. In the withdrawal re-

lease, the Commission suggested factors management should consider in evaluating the adequacy of internal accounting controls.

In conclusion, the Commission recognizes that the Foreign Corrupt Practices Act has spawned unintended problems for American business abroad and uncertainties concerning compliance with the accounting provisions. While the Commission will continue to apply the existing statute consistent with the policies developed over the past 4 years, the Commission supports changes such as those set forth in its testimony on S. 708 before the Senate Banking Committee.

Thank you.

[Testimony resumes on p. 157.]

[Mr. Shad's prepared statement follows:]

WRITTEN STATEMENT OF THE
SECURITIES AND EXCHANGE COMMISSION
SUBMITTED TO THE SUBCOMMITTEE ON TELECOMMUNICATIONS, CONSUMER
PROTECTION, AND FINANCE OF THE
HOUSE COMMITTEE ON ENERGY AND COMMERCE
WITH RESPECT TO THE COMMISSION'S ADMINISTRATION AND
ENFORCEMENT OF THE FOREIGN CORRUPT PRACTICES ACT OF 1977

November 18, 1981

The Securities and Exchange Commission appreciates the opportunity to participate in these hearings concerning the Foreign Corrupt Practices Act of 1977 ("FCPA"). This statement describes the events which led to enactment of the statute and the manner in which the Commission has administered and enforced the Act. We have also attached copies of the Commission's testimony before subcommittees of the Senate Committee on Banking, Housing and Urban Affairs with respect to S. 708, a bill which Senator Chafee has introduced to amend and clarify the Act. As that testimony indicates, the Commission supports S. 708 with certain limited amendments.

The Commission recognizes that the Foreign Corrupt Practices Act has spawned unintended difficulties for American commerce abroad and uncertainties concerning compliance with the accounting provisions. As the unanimous enactment of the Foreign Corrupt Practices Act in 1977 demonstrated, Congress was seriously concerned over the 450 instances of questionable corporate payments, both at home and abroad, that were disclosed pursuant to the Commission's traditional

reporting requirements. However, new legislation often proves to contain unanticipated ambiguities and is subject to differing constructions. The Commission has recognized that the Foreign Corrupt Practices Act has generated a substantial degree of consternation among businessmen of utmost good faith. 1/ For that reason, the Commission has attempted to afford guidance concerning its interpretation of the accounting provisions, 2/ to coordinate our activities with the Justice Department's efforts to afford guidance concerning the bribery prohibitions, 3/ and to apply the Act only to clear-cut violations.

The FCPA consists of two parts. The accounting provisions of the Act, which were added as Section 13(b)(2) of the Securities Exchange Act, require issuers: (a) "to make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer"; and (b) "to devise and maintain a system of internal accounting controls sufficient to provide

1/ Securities Exchange Act Release 17500 (Jan. 29, 1981), 46 F.R. 11544 (Feb. 9, 1981), 21 SEC Docket 1466 (Feb. 10, 1981) (hereinafter the Commission Policy Statement).

2/ Id. See also Securities Exchange Act Release No. 15570 (Feb. 15, 1979), 44 F.R. 10964 (Feb. 23, 1979), 16 SEC Docket 1143 (Mar. 6, 1979); Securities Exchange Act Release No. 15772 (Apr. 30, 1979), 44 F.R. 26702 (May 4, 1979), 17 SEC Docket 421 (May 15, 1979); Securities Exchange Act Release No. 16877 (June 6, 1980), 45 F.R. 10134 (June 13, 1980), 20 SEC Docket 310 (June 24, 1980).

3/ Securities Exchange Act Release No. 17099 (Aug. 28, 1980), 45 F.R. 59001 (Sept. 5, 1980), 20 SEC Docket 1258 (Sept. 16, 1980).

reasonable assurances that * * * certain statutory objectives are met. 4/ Most of the Commission's work with respect to the Foreign Corrupt Practices Act has involved the accounting provisions, and this statement first reviews the Commission's administration of those requirements. That administration has included rulemaking proceedings, 5/ a disclosure proposal, 6/ and the issuance of a statement of policy with respect to the accounting provisions. 7/ In addition, the Commission has brought 14 enforcement actions involving the accounting provisions. Finally, last June, the Commission endorsed S. 708 and certain additional proposed amendments to the accounting provisions designed to:

- (a) afford corporate management greater latitude in determining the cost-effectiveness of controls;
- (b) provide corporations greater protection against liability for violations without senior management's knowledge or involvement;
- (c) revise certain terms to reduce ambiguities and conform them more closely to accounting and securities law terminology; and
- (d) protect the confidentiality of certain business records.

4/ These objectives are related to the authorization and recordation of transactions and the safeguarding of assets.

5/ See Securities Exchange Act Release No. 15570, supra.

6/ See Securities Exchange Act Release No. 15772, supra.

7/ See Securities Exchange Act Release No. 17500, supra.

This statement also reviews the Commission's administration and enforcement of the foreign bribery prohibition set forth in Section 30A. The bribery prohibition has proved to be a less important part of the Commission's enforcement authority. To date, the Commission has brought only two enforcement actions under this provision. The Commission's administration of the bribery prohibition has also included a request for public comment concerning the impact and operation of Section 30A, 8/ and the issuance of a statement of enforcement policy indicating that the Commission would take no enforcement action under Section 30A with respect to any transaction where an issuer has sought and obtained clearance for the transaction from the Justice Department pursuant to Department's FCPA Review Procedure. 9/ As indicated in our testimony on S. 708, the Commission does not object to consolidation in the Department of Justice of authority to enforce the foreign bribery prohibition.

8/ See Securities Exchange Act Release No. 16593 (Feb. 21, 1980), 45 F.R. 12574 (Feb. 26, 1980); 19 SEC Docket 691 (Mar. 4, 1980).

9/ See Securities Exchange Act Release No. 17099, *supra*; Securities Exchange Act Release No. 18225 (Nov. 12, 1981).

I. The Genesis of the Accounting Provisions

The accounting provisions of the Act had their genesis in 1973 with disclosures that corporate funds had been used for illegal domestic political contributions. Subsequent Commission investigations and enforcement actions revealed instances in which questionable or illegal payments -- both foreign and domestic -- had not been disclosed to the investing public.

A. The Voluntary Disclosure Program

In response to the information that the Commission had uncovered with respect to questionable payments, the Commission developed a voluntary disclosure program in the summer of 1975 as a supplement to its enforcement program. The voluntary program was announced in several public statements, including the testimony of Commissioner Philip A. Loomis on July 17, 1975, before the Subcommittee on International Economic Policy of the House Committee on International Relations and the testimony of former Commission Chairman Roderick M. Hills before the Subcommittee on Priorities and Economy in Government on January 14, 1976.

Companies participating in this program were encouraged to conduct careful investigations of their operations under the auspices of persons who were not involved in questionable activities, and to discuss the question of appropriate disclosure of these matters with the Commission's staff before filing any

document with the Commission. Since the program was announced, more than 450 companies have disclosed information relating to questionable activities in filings with the Commission.

B. The Commission's Report on Questionable and
Illegal Corporate Payments and Practices

On May 12, 1976, the Commission submitted a "Report on Questionable and Illegal Corporate Payments and Practices" (the Commission's Report) to the Senate Committee on Banking, Housing and Urban Affairs. That Report, which was based on evaluation of public disclosures made by 95 companies with respect to questionable payments and practices, described the Commission's activities with respect to such payments and practices during the previous three years. It also analyzed various factors that might affect a determination as to whether such payments and practices are "material", and as a result, required to be disclosed to investors 10/, and set forth certain legislative and

10/ In TSC Industries, Inc. v. Northway, 426 U.S. 438, 449 (1976), the Supreme Court stated that the materiality standard requires:

"a showing of a substantial likelihood that, under all the circumstances, the omitted fact would have assumed actual significance in the deliberations of the reasonable shareholder. Put another way, there must be a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available."

other responses that the Commission recommended as a response to the problem.

In detailing the Commission's findings with respect to the corporate payments cases that had come to its attention, the Commission's Report concluded:

"The almost universal characteristic of the cases reviewed to date by the Commission has been the apparent frustration of our system of corporate accountability which has been designed to assure that there is proper accounting of the use of corporate funds and that documents filed with the Commission and circulated to shareholders do not omit or misrepresent material facts." 11/

As described by the Report, the "most devastating disclosure" resulting from the Commission's inquiry was "the fact that, and the extent to which, some companies have falsified entries in their own books and records * * *." 12/ The Commission's Report also found a number of other practices associated with the making of questionable or illegal payments, including the "accumulation of funds outside the normal channels of financial accountability, placed at the discretion of one or a very small number of cor-

11/ The Commission's Report at a (emphasis added).

12/ Id. at 58 and a. The Commission's Report stated (Id. at 13) that, as of the date of the Report, "virtually all questionable payment matters have involved the deliberate falsification of corporate books or records which, among other things, prevented these practices from coming to the attention of the company's auditors, outside directors and shareholders." The Report also concluded (Id. at a) that "falsification of records has been known to corporate employees and often to top management * * *."

porate executives not required to account for expenditures from the fund", the use of "non-functional subsidiaries and secret bank accounts" and the use of various methods of "laundering" or other means of disguising the source of funds used for such payments or the purposes for which they were disbursed. 13/

In brief, the Commission reported that its inquiry had revealed instances in which there had been inadequate accounting for the use of corporate funds and breakdowns in company systems of internal accounting controls. The Commission concluded that these were matters of concern irrespective of the existence of bribery or questionable payments because they "cast doubt on the integrity and reliability of the corporate books and records which are the very foundation of the disclosure system established by the federal securities laws. 14/

Thus, while the accounting provisions were "intended to operate in tandem with * * *" the bribery prohibitions of the FCPA to deter corporate bribery, 15/ the deterrence of such bribery by the accounting provisions was intended to be just one of the results that would flow from improved recordkeeping and systems of internal accounting controls. From the Commission's perspective, the principal purpose of the accounting provisions was to provide a greater measure of assurance that corporate

13/ Id. at 23-24.

14/ Id. at 3; see id. at b and 58.

15/ See S. Rep. No. 114, 95th Cong., 1st Sess. 7 (1977).

records will be made and kept in a manner that permits companies to fulfill their disclosure obligations under the federal securities laws.

II. The Commission's Rulemaking Proceedings and Related Efforts to Provide Guidance With Respect to the Accounting Provisions

The Foreign Corrupt Practices Act became law on December 19, 1977. The Commission's first action following enactment was the issuance of a release to inform issuers of the substance of the Act. ^{16/} The release also pointed out that, although "the legality or illegality of a particular transaction is one of the factors that must be assessed in determining its materiality" for disclosure purposes, the FCPA "does not alter the existing obligation of * * * companies adequately to disclose material questionable and illegal corporate payments and practices." ^{17/}

A. The Promulgation of Regulation 13B

The Commission promulgated two rules in February, 1979, as Regulation 13-B. Rule 13b2-1 prohibits the falsification of corporate books and records, while Rule 13b2-2 prohibits the making of materially false or misleading statements to an accountant in connection with an audit or the filing of required

^{16/} Securities Exchange Act Release No. 14478 (Feb. 16, 1978), 43 F.R. 7752 (Feb. 24, 1978), 14 SEC Docket 180 (Feb. 28, 1978).

^{17/} See n. 10, supra p. 6

reports. These rules, which had been published for public comment on January 19, 1977, 18/ were analogs to the Commission proposals for legislation that were not incorporated in the FCPA.

The Commission stated that the rules were promulgated for the following purposes:

to assure that an issuer's books and records accurately and fairly reflect its transactions and dispositions of assets; to protect the integrity of the independent audit of issuer financial statements that is required under the Securities Exchange Act * * * and existing Commission rules; to promote the reliability and completeness of financial information that issuers are required to file with the Commission, or disseminate to investors, pursuant to the Securities Exchange Act; to promote compliance with * * * [the accounting provisions]; and to prevent the concealment of questionable or illegal corporate payments and practices. 19/

In promulgating Regulation 13B, the Commission also set forth its views with respect to the applicability of materiality and scienter limitations to the accounting provisions. The Commission pointed out that the accounting provisions are not exclusively concerned with the preparation of the financial statements. Accordingly, the Commission concluded that the accounting provisions might provide "an independent basis for enforcement action by the Commission, whether or not violation

18/ Securities Exchange Act Release No. 13185, (Jan. 19, 1977); 11 SEC Docket 1514 (Feb. 1, 1977).

19/ Securities Exchange Act Release No. 15570, supra.

of the provisions may lead, in a particular case, to the dissemination of materially false or misleading information to investors." With respect to scienter, the Commission noted that the accounting provisions contain no indication that the Congress intended to include such a limitation in the statute.

B. Consideration of a Proposal to Require Management Reports on Systems of Internal Accounting Controls and Guidance to Issuers Concerning Such Systems

In a second rulemaking proceeding, commenced in April, 1979, the Commission proposed a rule that would have required each issuer to include a statement of management concerning the adequacy of the company's system of internal accounting controls in its annual reports on Form 10-K. 20/ The Commission stated that information regarding the adequacy of an issuer's system of internal accounting control might be necessary to enable investors to better evaluate the reliability of interim financial statements and other unaudited financial information, as well as management's performance with respect to the management and safeguarding of the assets of the business.

The Commission's proposal evoked a substantial public response. Over 950 individuals and organizations submitted comments, more than 90% of which were negative. After

20/ See Securities Exchange Act Release No. 15772, supra.

considering the views expressed, the proposed requirement was withdrawn in June, 1980. 21/ The Commission's withdrawal of the rule proposal was based, in part, on a determination that voluntary private-sector initiatives with respect to public reporting on internal accounting controls had been significant and should be allowed to continue. The Commission encouraged further voluntary initiatives, and indicated that it would monitor progress and revisit the subject within three years. 22/

C. The Commission's Statement of Policy
Concerning the Accounting Provisions

On January 13, 1981, the Commission issued a statement of policy concerning the accounting provisions of the FCPA. 23/ The policy statement expressed the view that uncertainty concerning the scope and meaning of the Act could have a debilitating effect on efforts to comply with the statute. It also recognized that "business resources may have been diverted from more productive uses to overly-burdensome compliance systems which extend beyond

21/ Securities Exchange Act Release No. 16877, supra.

22/ In withdrawing this proposal, the Commission noted that there are limitations upon the effectiveness of any system of internal accounting controls; that the reasonable assurances standard reflects a recognition that "it is not in the interest of shareholders for the cost of internal accounting controls to exceed the benefits thereof"; and that, because the relative costs and benefits will in many cases be incapable of precise quantification, "many decisions on reasonable assurance will necessarily depend in part on estimates and judgments by management * * *". Id.

23/ See Securities Exchange Act Release No. 17500, supra.

the requirements of sound management or the policies embodied in the Act." Accordingly, the Commission set forth certain views and policies that had been developed in the three years since the statute was enacted:

Reasonableness Standard. The Commission stated its view that the "reasonable detail" standard does not mandate absolute exactitude in recordkeeping, nor does the "reasonable assurances" standard require achievement of an ideal system of internal accounting controls. Instead, the Commission recognized that the concept of reasonableness tolerates certain deviations from the ideal and encompasses cost-benefit analysis.

Deference to Judgments Made by Corporate Management. The policy statement asserted that the accounting provisions "justify * * * deference to [management] decisions concerning corporate records and [internal accounting] control mechanisms." The Commission stated that the issuer "need not always select the best or the most effective control measure * * *" as long as the one selected is reasonable under the circumstances.

State of Mind. The Commission stated that the principal purpose of the accounting provisions "is to reach knowing or reckless conduct."

Status of Subsidiaries. The Commission took the position that, where an issuer controls more than 50% of the voting securities of a subsidiary, the issuer would be held responsible for subsidiary compliance with the accounting provisions. Similarly, if the issuer owned between 20% and 50% of the voting securities of the subsidiary, it would be responsible for subsidiary compliance subject to a demonstration by the issuer that its ownership does not amount to control over the subsidiary. In cases where the issuer owned less than 20% of the voting securities of a subsidiary, the issuer would have no responsibility for subsidiary compliance, unless the Commission could demonstrate control in fact.

III. The Commission's Enforcement of the Accounting Provisions

The Commission has brought fourteen enforcement actions under the accounting provisions since the FCPA was enacted. These enforcement actions include thirteen injunctive actions and one Commission administrative proceeding. In ten of these enforcement actions, all of the defendants or the respondent involved consented to settlement of the case, without admitting or denying the Commission's allegations. 24/ At the present time, three of the injunctive actions are pending with respect to at least one defendant. 25/

Violations of the accounting provisions have generally been uncovered in connection with inquiries into possible violations of other provisions of the federal securities laws. In addition, each case involved allegations that the corporate defendant violated one or more provisions of the federal securities laws. These include the antifraud provisions, the periodic reporting requirements, and the proxy provisions contained in Sections 10(b), 13(a), and 14(a) of the Securities Exchange Act, and applicable Commission rules promulgated thereunder. The

24/ In one other case, the consent of the defendant to settlement did not contain an explicit statement that the consent was without admitting or denying the Commission's allegations.

25/ The pending cases are SEC v. El Dorado International, Inc., et al. (D.D.C., Civil Action No. 81-0532, commenced Mar. 5, 1981); SEC v. World-Wide Coin Investments Ltd. (N.D. Ga., Civil No. C-81-1642A, commenced Aug. 31, 1981); and SEC v. Tiffany Industries, et al. (E.D. Mo., Civil Action No. 81-CIV-1106-C, commenced Sept. 10, 1981).

amounts of corporate funds involved in these cases has ranged from at least \$110,000 in a case alleging unauthorized management perquisites 26/ to in excess of \$23 million in a case involving allegations of accounting deficiencies related to questionable or illegal payments made prior to the effective date of the FCPA. 27/

Virtually all of the defendants that have agreed to settlements have consented to the entry of permanent injunctions against future violative conduct. Additional equitable relief granted upon consent has included orders of disgorgement in three cases, the appointment of three audit committees, and orders that four internal investigations be conducted and reports prepared concerning the matters alleged in the Commission's complaint.

26/ See SEC v. Marlene Industries, et al. (S.D.N.Y., 79 Civ. 1969, commenced Apr. 17, 1979).

27/ See SEC v. International Systems & Controls Corp., et al. (D.D.C., Civil Action No. 79-1760, commenced July 9, 1979).

Although most cases have alleged violations of both the recordkeeping requirement and the internal accounting controls provisions, three of the injunctive actions have been limited to the alleged violations of the recordkeeping requirement. In contrast, the violation of the accounting provisions found in the administrative proceeding was limited to the internal accounting controls requirement.

The cases have involved improper accounting with respect to four categories of conduct: (a) questionable or illegal payments; (2) exaggeration of company sales and assets, or the failure to keep adequate records of business transactions; (c) misappropriation or diversion of corporate assets in cases that have not involved questionable or illegal payments; and (d) unauthorized management perquisites. Please bear in mind, however, that the following discussion is limited to aspects of the cases that involved the accounting provisions; it reflects only a portion of the violative conduct alleged in the various complaints.

A. Questionable or Illegal Corporate Payments

Three of the fourteen actions to enforce the accounting provisions have involved questionable or illegal payments. Two of these cases alleged improper accounting, after enactment of the FCPA, with respect to payments to foreign officials that were made prior to enactment of the statute. In contrast, no cases have been brought to date under the accounting provisions in connection with payments to foreign officials made since the bribery prohibition of the FCPA became effective. ^{28/} The third case in this category involved payments that are not covered by the bribery prohibition.

^{28/} Neither of the two cases that the Commission has brought to enforce the bribery prohibition, which the FCPA added as Section 30A of the Securities Exchange Act, has involved violations of the accounting provisions.

In SEC v. International Systems & Controls Corp., et al., (D.D.C. Civil Action No. 79-1760, commenced July 9, 1979), the Commission alleged, among other things, that the corporate defendant (ISC) paid more than \$23 million through one or more subsidiaries to certain foreign persons and entities (including senior government officials and their associates) in order to assist the company in securing contracts. In this context, the Commission alleged that ISC violated the recordkeeping requirement by disguising such payments on its books and records as "consulting fees," "consulting services," "agent's fees," or "commissions". With respect to the internal accounting controls provision, the Commission alleged that ISC violated the statute by failing to devise and maintain a system of internal accounting controls sufficient to provide "reasonable assurances" that transactions would be properly recorded because it lacked vouchers, expense statements, and similar information documenting the nature of the activities or services for which certain expenditures were made.

In SEC v. Page Airways, Inc., et al. (D.D.C., Civil Action No. 78-0656, commenced Apr. 12, 1978), the Commission alleged that the corporate defendant (Page) and six individual defendants paid in excess of \$2.5 million of the corporation's funds to officials of foreign governments, to entities controlled by such officials or to purported agents as part of their efforts to sell certain aircraft and spare parts. The Commission alleged that Page violated the recordkeeping requirement because it "disguised and concealed" payments to government officials and other payments

through false, incomplete and misleading entries in its books and records which did not reflect the true nature and purpose of the transactions involved. Another alleged violation of the record-keeping requirement involved the failure to record receipts and disbursements of substantial amounts of cash. The complaint also alleged that Page violated the internal accounting controls provision because many expenditures were effected without adequate documentation and controls to ensure that expenditures were made for the purposes indicated and without adequate records and controls to document that the services provided in return for expenditures were commensurate with the amounts paid.

In SEC v. Crown Cork & Seal Co., Inc., (D.D.C. Civil Action No. 81-2065, commenced Sept. 2, 1981), the Commission alleged that the company (Crown Cork) made 42 payments to another corporation from October 1970 through October 1978, which amounted to approximately \$5.9 million. It was further alleged that the other corporation was controlled by an individual who was a senior officer of one of its major customers; that the payments were recorded by Crown Cork as competitive allowances, discounts or rebates; and that approximately \$5.1 million was diverted to the benefit of the individual that controlled the other corporation. The complaint alleged that Crown Cork violated the recordkeeping requirement because it was reckless in not knowing that the

payments were for the personal benefit of the individual involved rather than the purposes stated. 29/

B. Exaggeration of Sales and Assets, or the Failure to Keep Adequate Records of Business Transactions

Another area of enforcement action has involved improper accounting for business transactions and dispositions of assets in situations that do not involve questionable or illegal payments. Six cases are in this category.

In SEC v. Torotel, Inc., et al., (W.D. Mo., Civil Action No. 81-CIV-0116-CV-W-4, commenced Feb. 13, 1981), the Commission alleged that the corporate defendant and its subsidiaries routinely counted sales occurring after the end of an interim quarter as net sales for the quarter already ended, resulting in a material misstatement of revenues in interim consolidated financial statements between April 1, 1977 and the date of the complaint. The Commission alleged that false documents were generated in furtherance of this scheme -- including false customer invoices, production records, shipping records, inventory transfers and computer runs of accounting and shipping data -- in order to create the appearance that goods shipped subsequent to the interim

29/ The Commission filed a separate complaint against the individual involved, which is pending. The complaint in that case alleges violations of the antifraud and proxy provisions of the Securities Exchange Act, and certain rules promulgated thereunder, and also seeks disgorgement.

quarter had instead been completed and shipped before the quarter's calendar end. It was further alleged that the improper recognition of revenues in connection with this conduct resulted in material misstatements of the company's revenues by amounts ranging from \$200,000 to \$813,000 for each quarter involved.

In SEC v. Tiffany Industries, et al., (E.D. Mo. Civil Action No. 81-CIV-1106-C, commenced Sept. 10, 1981), the Commission alleged that Tiffany and certain senior officers violated the recordkeeping requirement and Commission Rule 13b2-1 by creating false records -- including backdated purchase orders, forged letters concerning the status of purchase orders, and improper adjustments with respect to inventory -- as part of a scheme to exaggerate its sales and assets. As a result, the complaint alleged that the company's financial statements for 1976 overstated sales by at least \$4.1 million and net income before taxes by at least \$4.3 million, while its financial statements for 1977 overstated sales by at least \$4.4 million and net income before taxes by at least \$3.0 million. 30/ This case is pending with respect to two of the individual defendants.

In SEC v. Computer Communications, Inc., (D.D.C. Civil Action No. 81-2590, commenced Oct. 19, 1981), the Commission alleged that the corporate defendant and certain company officers

30/ The complaint also alleged that Commission Rule 13b2-2 was violated because certain forged documents and other false records were provided to Tiffany's auditors during the course of an examination of the company's financial statements.

violated the recordkeeping requirement of the statute by recording revenue and income with respect to transactions that had not yet been consummated. In some cases, according to the complaint, revenues and income were recorded where a customer had done nothing more than indicate an intention to purchase equipment.

The complaint alleged, among other things, that this activity was part of a scheme to conceal the deteriorating financial condition of the company prior to a \$3.5 million public offering; the registration statement disseminated in connection with the offering was alleged to overstate revenues for the fourth quarter of 1978 by \$3 million and net income for the same period by more than \$400,000. In addition, it was alleged that these practices continued after the public offering and thereby inflated the revenues and income reflected in annual and quarterly reports filed with the Commission. 31/

In SEC v. World-Wide Coin Investments, Ltd. (N.D. Ga., Civil Action No. C-81-1642A, commenced Aug. 31, 1981), which is pending with respect to all of the defendants named in the Commission's complaint, the Commission alleged that the company violated the recordkeeping requirement by failing, among other things, to keep general ledgers and journals with respect to its

31/ The complaint also alleged that certain corporate officers violated Commission Rules 13b2-1 and 13b2-2 in connection with the foregoing conduct by falsifying, or causing the falsification of, company books and records and by making materially false and misleading statements to accountants in connection with their audit of the company's financial statements and the preparation of required reports.

transactions. The complaint also alleged violations of the internal accounting controls provision on the ground that there was no documentation of certain purchases and sales of assets, inadequate controls over access to inventory and assets, and a lack of documentation with respect to more than \$1.7 million of cancelled checks drawn to cash, to the person who was its president, chief executive officer and chairman of the board or to affiliates of that person. In this context, the Commission alleged that employees were allowed to write checks and remove cash and inventory from the premises without approval, and/or without documenting the purpose of the fact of the transactions involved. ^{32/}

In SEC v. Data Access Systems, Inc., et al., (D. N.J. Civil Action No. 81-3362), the Commission alleged that an individual defendant violated Section 13(b)(2) and Commission Rule 13b2-2 by making, or causing the making of, materially false and misleading statements to accountants in connection with audits or examinations of the financial statements of the principal corporate defendant. In this context, although the principal corporate defendant was not alleged to have violated Section 13(b)(2), the complaint alleged that it accounted for certain kinds of transactions, amounting to approximately \$27 million, as "sales" and that such

^{32/} The Commission also alleged violations of Commission Rules 13b2-1 and 13b2-2 in this case.

treatment was improper because the company remained at risk in the transactions involved. The complaint also alleged that company's auditors were unaware of documents which evidenced such risk and that company representatives falsely represented that the company had no continuing obligations or contingent liabilities. It was further alleged that, as a result of the manner in which these transactions were reflected, the company overstated its pre-tax earnings by a total of approximately \$8.1 million for its 1978, 1979 and 1980 fiscal years and understated its liabilities by approximately \$17.1 million as of February 1981. 33/

C. Misappropriation or Diversion of Corporate Assets

Three of the Commission's enforcement actions have involved the misappropriation or diversion of substantial amounts of company assets by corporate officers. The sums alleged to have been misappropriated since the enactment of the FCPA amount to a total of approximately \$5.8 million.

In SEC v. John E. Marqusee and Sheldon Lubitz, (S.D.N.Y. 80 Civil 2289 GLG, commenced May 6, 1980), the Commission alleged that the defendants engaged in a scheme by which \$3,270,000 in assets was diverted from Atlantic Improvement Co. (\$1.6 million after the effective date of the FCPA) to another company owned by Defendant Marqusee and his family. The complaint alleged that

33/ In SEC v. Wyoming Coal Corporation, et al., (D. Wy., Civil Action No. C-79-312, commenced Oct. 15, 1979), the Commission alleged that the company violated both the recordkeeping requirement and the internal accounting controls provision. However, the complaint parallels the language of the statute and does not provide details as to the nature of the conduct involved.

defendants caused Atlantic to maintain false and misleading books, records and accounts and prevented the company from devising and maintaining an adequate system of internal accounting controls. ^{34/}

In SEC v. Aminex Resources Corp., et al., (D.D.C. Civil Action No. 78-0410, commenced Mar. 9, 1978), the Commission alleged that Aminex, aided and abetted by a defendant who was its president, chief executive officer, and a director, "misappropriated and diverted at least \$1.24 million of corporate assets." The complaint alleged that the recordkeeping provision was violated because the misappropriations were disguised "by means of false and improper accounting in the books and records of Aminex." The complaint also alleged that Aminex violated the internal accounting controls provision because it failed to devise an adequate internal accounting control system to monitor corporate transactions and dispositions.

In SEC v. El Dorado International, Inc., et al., (D.D.C. Civil Action No. 81-0532, commenced Mar. 5, 1981), the Commission alleged that \$1,960,000 was diverted from El Dorado for the benefit of its chairman of the board and certain other corporations. The complaint alleged that the recordkeeping provision was violated

^{34/} The Complaint also alleged that the defendants violated Commission Rule 13b2-1 by falsifying the books, records and accounts of Atlantic and violated Rule 13b2-2 by making false and misleading statements to auditors in connection with the audit of the company's financial statements.

because the chairman of the board caused El Dorado to make and keep books, records and accounts that reflected the \$1,960,000 as "intercompany advances" when that sum was in fact "a non-interest bearing, uncollateralized advance to a non-affiliate * * *." This case is pending with respect to one defendant.

D. Unauthorized Management Perquisites

Two of the Commission's enforcement actions have involved the use of corporate assets for the personal benefit of corporate officials. These cases, involving what amounts to unauthorized management perquisites, include one injunctive action and one administrative proceeding.

In SEC v. Marlene Industries, et al., (S.D.N.Y., 79 Civ. 1969, commenced Apr. 17, 1979), the Commission alleged that the company paid sums to two individual defendants in excess of their annual compensation "without requiring any proof that such expenses were made for proper business purposes or that the corporation [would] be reimbursed for such expenditures." The complaint also alleged that the individual defendants used corporate credit cards for meals and then requested cash reimbursements for such meals, made payments for "purported business entertainment expenses without sufficient documentation" indicating the expenses were for corporate purposes and charged "corporate expenditures for personal goods and services" to various company and subsidiary accounts without adequately disclosing the nature of expenditures. 35/

35/ Although the complaint did not allege the amounts involved, the two defendants consented to repay the company a total of \$110,000.

The complaint also alleged that Marlene, aided and abetted by the individual defendants, violated the recordkeeping requirement because portions of the sums were "improperly recorded and reflected on Marlene's books and records * * *" and violated the internal accounting controls provision by failing to devise and maintain an adequate system of internal accounting controls.

The administrative proceeding was In the Matter of Playboy Enterprises, Inc., CCH Fed. Sec. L. Rep. ¶82,635 (Aug. 13, 1980). The Commission found that Playboy's audit committee had determined that officers and directors received in excess of \$2 million in personal benefits during an eight year period, and that unauthorized personal benefits amount to \$828,421 and 39,475 British pounds had been repaid to the company. In this context, the Commission found that Playboy violated Section 13(b)(2)(B) because it "lacked an adequate system of internal accounting controls for distinguishing between business and non-business * * * and between reimbursable and non-reimbursable expenses of officers."

IV. The Commission's Administration of the Bribery Prohibition

The Foreign Corrupt Practices Act charges the Commission with responsibility for civil enforcement of the prohibition against the bribery of foreign government officials by corporations registered with the Commission. This prohibition, which is contained in Section 30A of the Securities Exchange Act, has

been a less important part of the Commission's enforcement authority. To date, the Commission has brought only two enforcement actions under this provision. Each of these cases also included allegations of antifraud and disclosure violations and thus could have been maintained under the federal securities laws without reliance on Section 30A.

In SEC v. Sam P. Wallace Company, Inc., et al., (D.D.C. Civil Action No. 81-1915, commenced Aug. 13, 1981), the Commission alleged that the corporate defendant, a company engaged through wholly-owned subsidiaries in the construction business, made payments amounting to at least \$1.391 million to an unnamed foreign official in order to aid the company in procuring and maintaining certain contracts with an unnamed foreign government. The company and one of two individual defendants consented without admitting or denying the Commission's allegations, to the entry of permanent injunctions against further violative conduct. The company was also ordered to comply with an undertaking to appoint a special committee to investigate and report on the matters alleged in the Commission's complaint.

The other case was SEC v. Katy Industries, Inc. et al., (N.D. Ill. No. 78-C-3476, commenced Aug. 30, 1978). The Commission's complaint in Katy alleged that, in connection with obtaining a thirty-year oil production sharing contract with the oil and gas enterprise owned by the Indonesian government, Katy

entered into a contract to make payments to a Cayman Island corporation amounting to 13.33% of the annual net profits it received from the contract, while knowing or having reason to know that a high level Indonesian government official, and a representative of the same government official, would directly or indirectly share in the compensation. Although Katy was alleged to have made \$250,000 in payments prior to enactment of the FCPA, and no payments had been made since the effective date of the Act, it was alleged that Katy violated Section 30A based upon the contractual agreement, or promise, to make prohibited payments in the future. Katy and the individual defendants consented, without admitting or denying the allegations in the complaint, to the entry of permanent injunctions against further violative conduct. The company was also ordered to appoint a special committee of three directors to conduct an investigation and make a public report.

In response to reports that U.S. corporations were experiencing difficulty in conducting overseas business as a result of questions concerning the applicability of the prohibition in Section 30A, early in 1980, the Commission requested comments concerning the impact and operation of the bribery prohibition and the extent to which the law impeded legitimate foreign commerce. ^{35/} Unfortunately, however, the Commission

^{35/} See Securities Exchange Act Release No. 16593, supra.

received a limited response to this request. 36/ Affected persons may have been unwilling, despite the opportunity to request confidential treatment, to provide the Commission with information of this nature.

Despite the limited response, on August 28, 1980, the Commission issued a statement of enforcement policy under Section 30A, in which it declared, as a matter of prosecutorial discretion, that it would not commence an enforcement action where an issuer had sought and obtained clearance for that transaction under the Justice Department's FCPA Review Procedure. 37/ In issuing its statement, the Commission expressed the hope that its action would encourage greater participation in the FCPA Review Procedure, assist the Justice Department in providing a greater measure of predictability as to how the bribery prohibitions would be applied to particular cases, and lead to the development of a source of reliable data concerning the impact of the bribery prohibition on overseas business.

The Commission's traditional mandate with respect to issuers of securities is investor protection through full

36/ Only 14 comments were received in response to the Commission's request. See Securities Exchange Act Release No. 17099, supra.

37/ This Commission policy was recently extended. See Securities Exchange Act Release No. 18225, supra.

disclosure. The bribery prohibition has no direct nexus to that mandate. Accordingly, during the legislative debates preceding enactment of the Foreign Corrupt Practices Act, the Commission made clear that the prohibition of foreign bribery raised important issues of national policy unrelated to the objectives of the federal securities laws. For these reasons, then-SEC Chairman Hills recommended to the Senate Banking Committee that, if Congress chose to outlaw such transactions, it not do so under the federal securities laws. 38/ However, Congress decided to assign responsibility for civil enforcement of these prohibitions to both the Commission and the Justice Department, and criminal enforcement to the Justice Department.

Because the Commission's primary mission is disclosure, not substantive regulation of day-to-day commercial transactions, repeal of Section 30A would not impair the Commission's ability to administer the federal securities laws. In instances where foreign bribery involves a failure to disclose information which is material to investors, the Commission would retain its authority to take appropriate action. So long as the Commission has that authority, its principal role under the securities laws can be fulfilled. For these reasons, the Commission has testified that it does not oppose the provision of S. 708 which would transfer all enforcement authority with respect to Section 30A to the Department of Justice.

V. Conclusion

The Commission has endeavored to administer the Foreign Corrupt Practices Act in a reasonable and responsible manner. At the same time, the Commission recognizes that the Act has spawned confusion and uncertainty. While the Commission will continue to apply the existing statute consistent with the policies developed over the past four years, we support changes, such as those set forth in the Commission's testimony on S. 708 before the Senate Banking Committee. Legislation of that nature would clarify the law and relieve corporations of unnecessary compliance burdens without jeopardizing the objectives of the FCPA.

38/ Testimony of Roderick M. Hills, Chairman, Securities and Exchange Commission, Before the Senate Committee on Banking, Housing, and Urban Affairs, p. 9 (Mar. 16, 1977).

Mr. WIRTH. Thank you very much, Mr. Chairman.

Mr. Fedders or Mr. Greene, do you have any comment?

Mr. FEDDERS. I have nothing to add, thank you.

Mr. GREENE. Nor do I.

Mr. WIRTH. Mr. Shad, in going through your submission as it was sent up to us in draft form, I was struck by the number of questionable foreign payments cases and disclosures brought about before the enactment of the Foreign Corrupt Practices Act. You outline more than 450 instances of questionable payments and foreign bribery that were done before the act.

And we have had since the act became law just two bribery cases brought by the SEC in the last 4 years. Those are the proper numbers, are they not?

Mr. SHAD. The 450 are not all enforcement cases. That is the number of instances in which questionable payments were disclosed. In addition, these disclosures involved a wide range of conduct. They were not all situations involving bribery.

Mr. WIRTH. There were more than 450. That was the numbers that were used in your testimony.

Mr. SHAD. Yes.

Mr. WIRTH. What does this tell us about the act? Does this tell us that the Foreign Corrupt Practices Act has done a great job in preventing bribery?

Mr. SHAD. First, the disclosures by corporations did involve more than bribery, and particularly more than just foreign bribery. They also involved domestic slush funds and unaccountable utilizations of corporate assets.

There were actually about 50 enforcement cases brought between 1973 and 1977 by the SEC involving questionable payments in areas that the act was intended to address.

Also, the only serious study that I have seen is the SEC's own report in May 1976, which took 95 of the disclosures that had been made up to that time and provided an analysis of those disclosures. I will not burden you with that, but we have filed that report as well. If you want me to, I can amplify on the report.

Since enactment of the act, we have brought 16 cases. Fourteen have involved the accounting provisions, and two have alleged violations of the bribery prohibition. All of these cases could have been brought without the Foreign Corrupt Practices Act, under the existing disclosure requirements of the Federal securities laws.

However, the sanctions would not have been the same. The sanctions have required defendants to comply with the provisions of the act, and they do go beyond the existing disclosure requirements of the Securities Act and the Securities Exchange Act.

I do not have any factual basis to respond to your question if you want to compare the two numbers, the 50 cases brought during the 4 years before the act and the 16 cases brought since its enactment. There are various inferences that have been raised and conjectures.

Mr. WIRTH. How do you extrapolate from that? That is the question.

Mr. SHAD. I think that American business is very responsive to the Nation's laws. When the Foreign Corrupt Practices Act was placed on the books it had a dramatic impact in terms of efforts by business to comply. This conclusion is supported by the GAO Report concerning the act. That has been a principal cause of the concerns that has been raised, the indefiniteness of the act, which has caused business to be insecure as to what was necessary to comply. On the advice of counsel, they often refrain from acting simply because they do not want to get at cross-purposes with the Federal Government.

So it has had a significant, in my opinion, inhibitory influence.

Mr. WIRTH. Again, that is what we have been trying to document, and that is what the next hearing is all about. And it is very hard to get that kind of data other than anecdotes—we could not do this or we could not do that.

But nobody seems willing to say exactly what that is all about or to give us hard information on that. We are acting under assumptions and not hard data, and it seems to me that we spend an enormous amount of time in this Congress legislating on assumption and not legislating on data and facts, and that is something we should not do.

But the only data we have, you know, relates to the number of cases, and it seems to me that is one set of data that we have to look at. You look at that and try to draw inferences from that, that we had all of these cases beforehand and we have many fewer now.

One can draw, then, two inferences from that, either that the Foreign Corrupt Practices Act has been effective or that the SEC has not been aggressive in going after cases, right? I mean, it seems to me those are the two assumptions and I would assume that we would take the former and not the latter.

Mr. SHAD. Well, let me respond to part of the latter. There have only been two bribery cases brought under the prohibition of bribery that is administered by the commission. I want to point out that one of them involved acts before the Foreign Corrupt Practices Act, but because of continuing contractual arrangements it was brought under the bribery provisions.

The best objective source of information in terms of the reaction of business has been the GAO report. I think that has been a serious attempt to assess the response and reaction of industry.

Mr. WIRTH. Well, the GAO did an opinion survey on that front. They asked for the opinions of corporate officials and 55 percent of the companies did say that their compliance costs exceeded their benefits. And I want to get back into that.

It was a survey of opinion and not, again, of data or costs. An enormous number of respondents said it was their opinion the Foreign Corrupt Practices Act was effective in preventing foreign bribery.

So how do you extrapolate from that data? Do you have any response, Mr. Fedders, to the question of numbers of cases, what has happened in the last 4 years compared to what happened in the previous 4 years?

Mr. FEDDERS. There is no question that the act has had an impact as a deterrent effect on bribery as it relates to pre-FCPA conduct. There is no question that the act itself, the accounting provisions, have had an impact on the method by which public corporations maintain their books and records and establish their internal controls.

But there has been a cost. I would be one who would say that the cost has been enormous, enormous to corporations. Let us first take the accounting provisions. It has caused uncertainty as to whether an inadvertent violation would constitute a violation of the accounting provisions, concern as to what would constitute adequate internal controls, and concern as to whether specific conduct in connection with the sale of merchandise to foreign governments violates the antibribery provisions.

The uncertainty has not only been that of the businessman. When he turns to his lawyer or to his accountant and asks for advice, frequently the advice is qualified to the extent that the lawyer or the accountant says, look, I can give you a certain degree of guidance, but because of the uncertainty of the act, I cannot give you a clean opinion, or an unqualified opinion, that if you follow this course of conduct it may not be later challenged by either the Department of Justice or the Securities and Exchange Commission.

So my response is twofold: first, the act has had an impact and that impact has been enormous; but there has been a cost and the cost has been significant.

Mr. RINALDO. Mr. Chairman, do you yield on that point?

Mr. FEDDERS. I could engage in anecdotal stories with you based on my private practice before coming to the Commission, but they would do no more than frustrate you with more anecdotes and so I will restrain myself.

Mr. WIRTH. You understand the difference between trying to get a sense of what has really happened out there and a lot of anecdotes. We have been given all kind of information and have read

all sorts of reports that such and such company said that if this had happened they might have been able to do so and so, and then they say they might have gotten that particular kind of business.

Mr. FEDDERS. This is the greatest challenge that the committee has. If you look at the pre-FCPA history, there was a great reluctance on the part of the corporate community to come forward and comment on the proposed legislation. For being such an important act, the legislative history of the FCPA itself is very meager.

If you look now at the legislative history which you are developing in both from the House and the Senate as you move toward the consideration of amendments, it is still rather meager. I am hopeful that, whatever the end result, there will be substantial legislative history that will at least provide as better guidance to the corporate community, their lawyers and accountants.

Mr. WIRTH. That is exactly what we are trying to create here, an understanding of where it came from and what that history of the legislation is, what the enforcement has been and what the impact is. And that is why your submission was very, very helpful coming from the SEC, as was Justice's.

As I stated when we began this morning, the information from the Special Trade Representative and the information from Commerce and the information from State has not been forthcoming. It is difficult to do, as we try to create a thoughtful and good record, to do so without their input and information, other than saying, "Change the act and our assumptions are valid."

Well, let us look at those again. That is what we are trying to do.

It seems to me that you are exactly right. One of the problems was that we did not look as carefully as we should have, and let us do it now before we rewrite the act.

Mr. RINALDO. I would just like to follow up on the point that you made, which I think is very well taken, because in the Commission's policy statement on the accounting provisions that were issued in January, I believe, of this year, the Commission addressed specifically what you were speaking of, I believe, the state of mind required for liability under these provisions.

And the Commission stated in that report that, although the present statute does not require the Commission to demonstrate knowing misconduct, inadvertent recordkeeping mistakes will not give rise to Commission enforcement proceedings. So it then went on to say that enforcement proceedings or actions taken by the Commission have involved knowing or reckless conduct rather than inadvertent violations.

Now, I would like you to answer this question. It is tied in with the entire statement that you made. Do you have any objections to changing the statute to reflect present Commission policy to exempt inadvertent mistakes from liability? And how would you suggest that this be done most effectively and unambiguously?

Mr. SHAD. We supported your bill and Senator Chafee's. The two are identical, I believe.

Mr. RINALDO. Yes.

Mr. SHAD. We suggest a knowing and reckless standard, which is a much higher standard of proof be required of the Commission to enforce the act. This would respond to the question inadvertent of

conduct. In other words, in order to be held liable there would have to be a knowing or a reckless violation.

Mr. RINALDO. Thank you.

Mr. FEDDERS. Let me add one thing, Congressman. What you have articulated is how would we reflect our January policy statement in an amendment to the law. I think the answer is reflected in Chairman Shad's June 16 statement before the Senate in response to S. 708, and that is a lengthy statement. It is attached to our written submission, and contains the analysis that we went through in arriving at that determination.

Mr. SHAD. I would like to ask the General Counsel, Edward Greene, to amplify on that.

Mr. GREENE. The Chafee bill prohibited only knowing conduct. We suggested in our testimony that the standard be knowing and reckless. That approach would effectively implement the Commission's policy statement.

We also supported other changes. We did feel that the ambiguity in the accounting provisions was causing corporations to incur unnecessary expense. We think that recklessness is a standard that the courts are used to applying and would be appropriate in this area.

Mr. RINALDO. Thank you.

Mr. WIRTH. Mr. Collins.

Mr. COLLINS. Thank you, Mr. Chairman.

I am happy to see you emphasize the knowing and reckless standard. Many of my colleagues in the House have never been in business. They do not understand the complications, involved in day-to-day business operations and the possibility of making an inadvertent mistake.

The law has had an effect, there is no question about it. Businesses are to the point now where they are reluctant and timid about going after foreign business. The Japanese, Germans, French, and English do not have restraints similar to the act we are dealing with today.

Everywhere I look, I see other countries that are very aggressive. This law is just tremendous for them.

One other thing that concerns me is whether the nature of mistakes made by business are taken into consideration. Do you differentiate, does the law effectively differentiate between a very small and a very large item?

Mr. SHAD. No, it does not.

Mr. COLLINS. Do you think that there is some way we could do that?

Mr. SHAD. Well, we have suggested as a qualification of the Chafee-Rinaldo bill that the standard be that which a prudent businessman would apply in the management of his own affairs. The language of the bill at the present time concerning internal controls refers to controls sufficient to enable a company to record the disposition of its assets and its operations in accord with generally accepted accounting principles.

But even within generally accepted accounting principles, there is not really a hard definition of materiality. And the discussion during the Senate hearings related to whether materiality should be based on something sufficiently important so that it would

change a number in a published financial statement. Most companies publish their financials rounded off to millions.

The larger companies do not get into smaller amounts. And so if that were the standard, if there were no disclosure or accountability requirement with respect to an item that did not change a number in the financial statements, which is actually a tougher definition of financial materiality than was used, that would mean that a company that had a questionable transaction, such as a payoff to the son of the president or some other extremely abusive situation, the company would not necessarily be required to have a system of internal accounting controls geared to pick it up.

A \$990,000 questionable payment of that sort could be very material. If you were a stockholder of the company, would you want to support management that engaged in questionable payments that could get to that order of magnitude?

So it has been for that reason that our approach has been to suggest the so-called prudent man standard, which is the kind of controls that you would want in managing your own affairs.

Mr. COLLINS. Let me ask you something about a foreign subsidiary. I do not completely understand the way the law works, but suppose a parent company in the United States has a foreign operation over in Europe and they have no knowledge of unauthorized or illegal practices engaged in by that subsidiary. Are they, under current law responsible for the subsidiary's illegal practices?

Mr. SHAD. Yes.

Mr. COLLINS. Even if they do not know a thing in the world about them?

Mr. SHAD. Well, you see, what happens is those foreign operations are picked up in the consolidated financial statements. When you read any major company's annual report, you are getting numbers as to those foreign activities, along with all the rest of their activities. And if the foreign subsidiary is engaged in questionable activities, that is often in fact the grounds under which a lot of the cases arose.

Mr. COLLINS. What are some of the major types of questionable activities? Do cases of companies trying to expedite customs processes make up a large proportion of the cases?

Mr. SHAD. No. That is often referred to as a "grease" payment, and I think that the attitude is that these nominal payments to induce low-level Government employees to discharge their responsibilities are unfortunate but perhaps necessary in some cases; it is not uncommon to give someone a bottle of whiskey or something else of nominal value to get him to put a stamp on something moving across the border, because otherwise it could sit there for a long time.

I personally have known some of the companies that I have been on the boards of have made shipments in a suitcase of critical machinery because of a breakdown that was costing the company \$100,000 a week. Such a shipment could be held up at the border by some very junior customs agent. So I think that this is an area that generally has been acknowledged to be outside the scope of the act.

Mr. COLLINS. You are not prosecuting such cases?

Mr. SHAD. No, and nor does the proposed amendment.

Mr. COLLINS. It will leave out what they call the grease payments?

Mr. SHAD. Yes.

Mr. COLLINS. What then, would you say is the major problem companies are experiencing today that brings them into conflict with the law?

Mr. SHAD. Well, in some countries you are often required to do business through a foreign agent.

Mr. COLLINS. Yes, that is very real, because everyone knows that. In other words, they will tell you who a transaction has to clear through if you are going to do business. Is that illegal, to have to clear through that person?

Mr. SHAD. No. The question is whether he is a conduit for a questionable payment? Is it then going to end up in the hands of some government official, and is he merely a conduit?

The present statute focuses on whether the company had reason to know that funds would be paid to a foreign official by an agent—the implication being that you have to get behind it and find out what the agent does with the money. Under Congressman Rinaldo's proposed amendment to the bill, that language would be removed.

Mr. COLLINS. How could a company ever know what an agent does with money? And I know you are absolutely right, that in the Middle East—and that is well known everywhere—that you have to go to certain people, that they literally are the exclusive buying agent within that category.

Now how in the world could some American company know? You say the way it is now they are supposed to know? They have the responsibility of knowing?

Mr. SHAD. I had better let the general counsel amplify on that.

Mr. GREENE. Again, we have reason to know language creates one of the ambiguities in the Act. Does that suggest there is a duty of inquiry? If so, how far does it go? What evidence should put you on notice?

In this area and in the accounting area, more certainty is needed to avoid having to incur unnecessary costs either documenting the transaction or putting in systems of internal accounting controls. It is very hard in this area to get counsel to give you a clear opinion. Most businessmen like to proceed with advice of counsel that the transaction is legitimate or authorized. In this area it is almost impossible for counsel to give a clear, unambiguous opinion.

Mr. WIRTH. Would the gentleman yield?

Mr. COLLINS. Yes.

Mr. WIRTH. It seems to me that the other side of this is that if we amended the Foreign Corrupt Practices Act to limit the corporation's responsibility for paying bribes only where the corporation or its officers directed or authorized, in the language of the Rinaldo bill, a bribe, would we not be encouraging a kind of head-in-the-sand attitude, that we are not going to take responsibility as the corporation or the directors of the company, but you know, we are not going to authorize that which is illegal, so therefore our foreign agents can go ahead and do whatever they want to do and we will bury our heads in the sand and pretend it is not happening?

Is that not the other side of the exchange that you had with Mr. Collins?

Mr. GREENE. I am not sure that that would necessarily result. The Commission did not comment——

Mr. WIRTH. It could very well be the case.

Mr. GREENE. This is an area where it is very difficult in legislation to come up with a standard that will strike at the conduct you want to hit.

Mr. WIRTH. The point I am making is that to say "to direct or authorize" leaves open enormous room for mischief, does it not, mischief being errors of omission rather than errors of commission?

Mr. GREENE. That could happen. But the law does suggest that authorization can take various forms. I do not think you would necessarily have to show an explicit authorization. There may be a course of conduct that would satisfy a court that there was authorization.

Mr. WIRTH. You are the enforcement chief, Mr. Fedders. What is your reaction to that?

Mr. FEDDERS. Well, the first thing that is important to understand is that the reason to know language appears only in the anti-bribery provision; it is not contained in the accounting provisions.

The ambiguity of the reason to know provision has caused untold difficulties for corporations. The last act that I performed before I joined the Commission was to write a piece in "The Middle East Executive Report," that I shared with Ms. Cochran, detailing the difficulties that businessmen frequently have when doing business in a foreign country where an agent is employed in the transaction.

I articulated at length the kind of steps and procedures that I recommended that corporations employ as a prophylactic to make certain that they did not know or have reason to know. Those procedures were expensive and time-consuming. In response many people would say, if I have to pay you or if I have to undertake those responsibilities, I am losing much of the profit in the transaction, and I am also wasting a considerable amount of time, while my foreign competitors will be in a position to move forward.

My own view is that the elimination of the reason to know language does not necessarily represent a head-in-the-sand approach, although knowledge may not be a perfect standard here. There may be some middle ground. I have suggested that in the article that I provided to Ms. Cochran.

It is a difficult question. The proper balance, the wording of the legislation, is going to be terribly important. I think it is not only the words of the legislation that will be important, but the legislative dialog that goes on and discussion you put in your report on this particular topic.

I, for one, did experience considerable frustration since 1977 in trying to assist corporations to satisfy that reason to know standard. At the end of the negotiations, where they were about to sign the contract, I was never able to issue a clean opinion. There was always a slight qualification.

Businessmen, in these kinds of transactions, when you have the potential of criminal liability want, and I believe they deserve, some degree of certainty with regard to their conduct.

Mr. WIRTH. And they also get from counsel, obviously, a cautious opinion, which is the job that you in your previous incarnation were responsible for providing.

Can you tell me, Mr. Fedders, where the Foreign Corrupt Practices Act fits in the SEC's enforcement priorities? This is a question that relates not only to the priorities that you have, but also to the budget issue that we have talked about, Mr. Chairman, and the grave concern that members of this subcommittee have that you have the resources necessary to do the job that you are charged with doing.

Mr. FEDDERS. I would be glad to. The Foreign Corrupt Practices Act remains an important responsibility of the Commission. It is not one that the Commission exercises lightly. But it is not the kind of law that one enforces by having a specific program addressed to the Foreign Corrupt Practices Act. We have not established a team of lawyers or investigators who investigate Foreign Corrupt Practices Act violations.

The way case violations frequently arise are as collateral issues of other kinds of investigations. Chairman Williams commented on that in January in the Commission's policy statement. He said that there is no specific program addressed to Foreign Corrupt Practices Act type activities, but that these kinds of possible violations are confronted in the course of other investigations that are being conducted.

Now, the reason that this occurs is because we are primarily an agency involved in regulating the disclosures of corporations. We do not engage in audit activities. We do not go to corporations and audit their books and records, nor do we go and audit their internal controls.

We are concerned about their disclosure activities. Frequently, when coming upon a disclosure problem and engaging in additional investigation, as a collateral issue we may identify a books and records or an internal control problem and then pursue that matter in the investigation.

But I think our enforcement history and the cases that Chairman Shad has told you about demonstrate that, in each case where there has been an FCPA violation, there has also been a violation of one of disclosure provisions of the Federal securities laws, generally sections 10(b), 13, or 14 of the Securities Exchange Act and rules promulgated thereunder.

Mr. WIRTH. Does that not suggest that a lot of the accounting therefore is already done?

Mr. FEDDERS. I am sorry.

Mr. WIRTH. I mean if we are going to pick this up in terms of other requirements in the law, does that suggest that the requirements everybody says are so onerous coming out from FCPA are already accounting that companies do, in any case?

Mr. FEDDERS. Well, I am sure that there is a degree of compliance with the FCPA, if that is what you are saying. Certainly, the accounting profession and the legal profession have been concerned and have assisted corporations in attempting to comply with this Act.

But I think we must ask at what costs and with what degree of certainty. When they are all finished, do they know that their sys-

tems of books and records and internal accounting controls in fact comply with the law, or are there potential violations? It is that degree of uncertainty that I think we are really addressing today; the cost factor and the degree of uncertainty. Is the cost too high and is the uncertainty too great?

Mr. WIRTH. Let me come back to that if I might. Did you have something you wanted to add, Mr. Shad?

Mr. SHAD. The accounting has been done as you are suggesting. The question is whether it has been in adequate detail. Normally in our overall investigation of possible disclosure violations, we get into whether a company has adequate accounting controls and whether there are questionable payments involved.

Mr. WIRTH. Going back to the question of priorities, are you all, in looking at the budget, have you developed documents internal in the SEC defining what your priorities are, how you are going to go about meeting all of your responsibilities; what shifts are going on and how the FCPA fits into those priorities?

Mr. SHAD. Well, what we have done is consider specific allocations in the various divisions. For example, how would we trim personnel if we are required to reduce our personnel by 20 percent in order to accommodate the 12-percent budget cut. The area that would be cut the least would be enforcement.

In the general counsel's office, for instance, there would be a much more drastic cut. And certain publishing activities of the Commission, such as publication of statistics and reports for industry, would have to be cut drastically. Enforcement would be cut the least because we are essentially an enforcement agency.

It then becomes the Director of Enforcement's responsibility to figure out how, within his reduced budget, he would allocate those resources. I will ask John to amplify on that.

Mr. FEDDERS. Your specific question went to whether we have written any documents or prepared any memoranda with regard to how we would implement reductions, or what priorities we will emphasize in the future.

Most of this is contained in conversations with Chairman Shad, with the other commissioners, and with my own senior staff. At the same time, we are talking about those things that we ought to emphasize at the present time. As Chairman Shad has so well articulated, and I certainly agree, three of the main areas of focus today are insider training, manipulation, and fraud by reporting companies.

It is in the investigation of fraud by reporting companies that we come upon this collateral issue of the accounting provisions and the antibribery provision of the Foreign Corrupt Practices Act. So to the extent that we emphasize fraud by reporting companies, there is still the likelihood, the possibility, and the prospect, that we will uncover potential violations.

Mr. WIRTH. On the overall question of your budget, Mr. Chairman, I was encouraged that when the appropriations came to the floor of the House, the minority on the House side was only moving to a 5-percent level rather than 12 percent. And looking on the Senate side, the Senate Appropriations Committee in fact has come in—the Republican-controlled Senate, mind you, has come in with

an appropriation level higher than that proposed by a Democratic-controlled House.

So I think that perhaps those are signs that the only people thinking about 12 percent, if they seriously are at this point, are downtown. Looking at your budget to cut it 12 percent below the level proposed in March, there does not seem to be much stomach up here for doing that on either side. When we get out of this difficult veto situation at the end of the week, it is yet to be beheld by any of us in any of our incarnations.

But in any event, that, I believe, is the framework at this point.

Mr. RINALDO. Thank you, Mr. Chairman. We have talked about, I guess, proving over and over again the burdens and the problems that the act has caused. I'm sure there is no one here that condones bribery, wants to make it easy to bribe someone, but it is interesting that both the Carter administration and now the Reagan administration have expressed concern about the export disincentives caused by the Foreign Corrupt Practices Act, and about the unnecessary burdens that it has imposed on American companies.

I think really the key thing is do you agree that it has inhibited exports by American companies.

Mr. SHAD. I believe that, but we do not have objective evidence of it within the SEC.

Mr. RINALDO. I guess it is something that would be very, very difficult to prove.

Mr. SHAD. In the bribery area, we have only had two cases and they are not indicative of major foreign trade situations.

I wanted to add earlier, that is part of the reason why we were not in favor of being given the responsibility for enforcement of the foreign bribery provisions. We have no opposition to consolidating them within the Justice Department so that one agency will administer all of the bribery prohibitions.

Mr. GREENE. Congressman Rinaldo, we were concerned and put out a release asking companies to come forward to give us evidence of difficulties they may have experienced in complying with the bribery provisions.

Mr. RINALDO. Well, I think one of the problems there, and I do not think we should cover it up, is that when you ask for a company to come forward and tell you the problems they are experiencing, either to you or to this committee, a lot of the companies feel they are going to have to come forward and say here is what we were doing before, and here is what we have stopped, and possibly admitting to some violation of the act. They are not certain that they are even violating the act.

Under those circumstances, they prefer not to come forward.

Mr. GREENE. Since the evidence was so skimpy, we decided we would rely upon the Justice Department's FCPA Review Procedure. We said we would not bring any action with respect to a transaction if any company sought and received clearance for the transaction under that Review Procedure. We recognize this is a difficult area, and that people are unwilling to come forward. There is a problem, but we ourselves have not been able to develop the kind of evidence that we would like to have.

We are therefore prepared to rely on the Justice Department and defer to their judgment in this area.

Mr. RINALDO. Let me ask you this. Do you feel it is necessary to amend the act?

Mr. SHAD. Yes, we have proposed that and we stand here to support it. Let me add with respect to the comment that we will not pursue questionable payments that have been submitted to the Justice Department for their prior review. Interestingly enough, there have only been four such transactions cleared by the Justice Department. I guess you will get into that this afternoon. So although the Commission has said it will not pursue transactions if they are cleared by Justice, in fact, there have not been a lot cleared by Justice.

Mr. RINALDO. We recognize there are problems with the act. We have, you might say, peripheral evidence that it has acted as a disincentive as far as exporting goes by American companies.

You feel that the act can be amended. Can this be done without weakening the provisions prohibiting bribery of foreign officials?

Mr. SHAD. In all of our testimony we have not addressed that because we concur in the transfer of that responsibility to Justice. We felt that that is an area that they ought to be responsive to, not us.

Mr. RINALDO. In January of this year—and I am going back to that policy statement that you issued concerning the accounting provisions of the FCPA, and you wanted to aid companies in complying with the act's requirement.

That policy statement acknowledged that uncertainty concerning the scope and meaning of the act can have a debilitating effect on efforts to comply with the statute. Now, how binding is such a policy statement as you issued on a future Commission, for example?

Mr. SHAD. I think that is a very good question. I do not think it is binding. I do not think that you can say that a policy statement cannot be modified either by subsequent rulemaking procedures where you put out a new rule for comment, or by subsequent policy statements.

Mr. RINALDO. So if that is the case, what you are really saying, and the fact that the policy statement is subject to change by Commission action, then, in effect, what we are saying is that would continue the uncertainty that presently exists for companies seeking to comply with the act unless it is amended in a statutory manner.

Mr. SHAD. Yes.

Mr. RINALDO. What I am asking is, we need a statutory change in order to provide the certainty that companies desire and I feel are entitled to, in order to properly comply with the act.

Mr. SHAD. That is correct.

Mr. GREENE. The policy statement is a statement of prosecutorial discretion which could be changed. Second, if there were private litigation with respect to that act, it is not clear that the policy statement would be the way a court might interpret its provisions.

So there is still an area of ambiguity, notwithstanding the statement.

Mr. RINALDO. I just wanted to ask one more question that I am concerned about. When you testified before the Senate Banking Committee, you addressed several issues of concern to companies

who have to comply with the act, and you made recommendations for addressing those problems.

A major concern of the companies, as we know, is the cost of establishing and maintaining the internal accounting problems which are exorbitant.

Now, can you describe the current requirement of the law for considering the cost effectiveness of internal accounting controls, and exactly what your provisions or recommendations are for changing that provision?

Mr. SHAD. Yes. The present act does not contain language addressing the cost question. The Chafee bill proposes to include language in the statute to make clear that companies are only required to install internal accounting controls where the costs are expected to be less than the benefits.

In our analysis of that provision, we have gone further because you can have some uncertainty should a major company have to deal with a very close call as to whether the costs exceed the benefits.

In our proposed amendment to the Chafee-Rinaldo bill, we suggested language stating that companies should not be required to install the internal accounting controls and other systems unless the management believed the benefits would significantly exceed the costs. In other words, there should not be a question as what is or is not cost effective in this area. It should not be a close call.

Mr. RINALDO. You have also, as I understand, endorsed recommended changes for the current requirement of the law as far as liability for accounting violations by low and mid-level company officials, is that correct?

Mr. SHAD. Yes. In order to hold the issuer or the company liable, it should be with the knowledge or concurrence, or a failure to act appropriately on discovery, on the part of executives at a high level—say, the treasurer or vice president level or up—rather than at the clerical level.

Mr. RINALDO. I have no further questions.

Mr. WIRTH. We have to go over and vote, but I would like to make a quick announcement related to the schedule of the subcommittee.

We have scheduled today a markup on the tire bill which was pursuant to my interest in accommodating the interest of the gentleman from New Jersey, as we had had hearings on the VHF issue, and the New Jersey issue, and the Foreign Corrupt Practices Act.

In the past, we have had witnesses on the tire bill, and at that time the independent tire dealers said that a voluntary registration system would increase the number of people registered. That was their testimony.

Also at the hearing it was suggested by some that an automatic trigger provision be added to the Rinaldo bill. It was my feeling that that kind of a provision would be too extreme, and so I suggested a very simple compromise as an amendment to the Rinaldo bill that would go into effect only if the tire registration decreased dramatically rather than increased, as the tire dealers had predicted, consistent with what the tire dealers had suggested. Everyone,

including the manufacturers agreed that we should have lists of people who buy tires.

The question is how do we do that in a most cost-effective way, and that is one of the thrusts of your bill. So I put this cost-effective test in the amendment that I was offering so that tire dealers would not be overburdened in the future. It seemed to me this was a very simple amendment, but now, for reasons that I do not understand, it has created an enormous amount of controversy, and perhaps some confusion among the members of the subcommittee.

What we have attempted to do in the subcommittee—and we have not been very successful in doing it today—is to make sure that everybody understood what was in legislation and that everybody was in agreement. We have done that on every piece of legislation to date.

Consequently, because we do not have that agreement at this point, we are canceling the markup on the tire bill today until we get this one sorted out, which I think we are going to be able to do. So we will not—we will be coming back to you, if we might, Mr. Chairman, after we vote. I do not think that you are concerned about the enforcement of tire registration, Mr. Fedders. That is another part of our agenda, and I just wanted to make that announcement for now.

We will have to adjourn briefly and come right back.

Mr. RINALDO. Can I ask a quick question on that point, Mr. Chairman? I did not know until I arrived here this morning that the markup was canceled. When you say that we will have the markup after we sort out the problem, do you mean that we are going to have an informal meeting of the subcommittee members shortly to discuss the amendment that you proposed?

Mr. WIRTH. I think we will just have to look at the overall picture. When everyone gets onboard we will have a bill, and when they do not get onboard, we will not have a bill.

Mr. RINALDO. So you are saying you are going to hold the bill up unless—

Mr. WIRTH. What I am saying is this subcommittee operates in terms of people cooperating, and that is what I want to see and that is what we have had in the past, and we have been very successful in doing so, and I plan to continue to operate the subcommittee in that fashion.

Mr. RINALDO. Well, I do not see anything wrong with having a markup and a public discussion of a problem, because quite frankly, I do not object to the provision that you envision regarding a standardized registration form. I agree with your provision clarifying that tire manufacturers do not have to keep records which they do not receive.

My only problem with your entire amendment, in fact, was the provision that gives NHTSA authority to overturn the change in the law and return to the old law. I have not been able, quite frankly, in the short time in which I have seen it to find any statute that allows an agency to, in effect, legislate and go back to the old law. And perhaps we could compromise on that issue; I would be willing to go along with everything you have there, provided we change that one issue and have a report, for example, by NHTSA

within 2 years after the effective date of the law, and then sit down and reevaluate the law at that point; how it is working.

Mr. WIRTH. If, as the tire dealers have said to us, we will find a great number of increased registrations as a result of the voluntary program, that is just fine. And I think we would all like to see that happen, if it works.

If it does not work, then it seems to me we ought to have a remedy in the interest of people who are buying tires, and it appears that we still have to work that out. And that is what I would like to do.

Mr. RINALDO. Well, I just caution—I do not know about a trigger mechanism as being a really effective statutory or proper method of legislating. By putting a trigger mechanism in a law—

Mr. WIRTH. We trigger things on a steady basis. That is not inconsistent with any kind of past practices of the law. We can write the law any way we want to. Anyway, we will adjourn and come back very shortly.

[Brief recess.]

Mr. WIRTH. Mr. Shad, I think you had a brief clarification in response to an earlier question that you wanted to ask?

Mr. SHAD. Yes; it was in response to Congressman Rinaldo's question concerning cost effectiveness of the act, and I said that the present act does not have a cost-effectiveness language within it. In other words, language providing that the controls would only have to be established if they were cost effective.

And I was reminded during the break that while that is an accurate statement, the act does refer to providing "reasonable assurances" that certain statutory objectives will be met and the legislative history indicates that, under the reasonable assurances standards, the cost should not exceed the benefits.

In other words, there was some awareness that relative costs and benefits would be taken into account. This view is included in our statement of policy on the act.

Mr. WIRTH. Thank you. We were talking earlier about the costs and the benefits, and I said I wanted to come back to that and I would like to now.

There has been a lot of discussion and a number of statements made that the institution of accounting control systems called for by FCPA are not cost effective. There are arguments made.

In your earlier testimony to the Senate, which is included today in your submission to us, you said that management should not be required to change or improve its internal controls unless management determines that the economic benefits will significantly exceed the costs.

Mr. SHAD. Yes.

Mr. WIRTH. Then the question we get to is, we can determine those costs, you can measure what the costs are. How does a corporation go about weighing the benefits?

Mr. SHAD. The weighing of the benefits is difficult, but it involves both objective and subjective judgments that are not uncommonly made by management.

One of the most subjective areas, involves the advice of the accountants and lawyers to a company whether they would, in fact,

be in compliance. They must act on opinions rather than on hard facts.

Mr. WIRTH. So in other words, it is very hard to empirically say that something is or is not cost effective, right?

Mr. SHAD. To say it absolutely. That is why we suggested significantly language, so it would not be an issue unless in the judgment of management the benefits significantly exceeded it. This would avoid a close call situation.

Mr. WIRTH. That again lays in some of the ambiguities we are talking about here, similar to what we were discussing earlier with Mr. Fedders; how do you really identify empirically what it is we are talking about here. It is highly subjective and it is very difficult to be precise in terms of cost benefit.

The GAO report earlier this year talks about this as—well, let me read the quote from the SEC's response to the GAO report:

Even if there may be some excess costs on the basis of the calculation performed by an issuer for its own purposes, it should be recognized that the benefits to the nation in the form of more reliable disclosure to investment, improved accountability, greater confidence in the capital market system and the deterrence of bribery and other improper conduct are important considerations. To the extent that excess costs may be of a marginal nature, these benefits might be viewed by the Congress as justifying cost.

Again, there are a number of variables in there to be measured. As you look at benefit you can measure the cost, and then there are a variety of things that have to be looked at in terms of benefit, which are, you know, very subjective.

Mr. SHAD. I would not disagree with what you have just said.

Mr. COLLINS. Mr. Chairman, would you yield?

Mr. WIRTH. Go ahead, please.

Mr. COLLINS. I had two or three things I wanted to bring up at this time. First, I want to go back to the budget. As you know, over here in the House, the Democrats have a majority of 50 votes, so we are discouraged over here.

Our chairman mentioned that the Senate was reluctant to take firm action. This matter of cutting the budget is of paramount concern. The reason we do not understand it on the Hill is that we stay in session too much. I have a bill on that. If Members of Congress went home and talked with the folks at home, they would know that we have too much government in this country. If you go to New York or Dallas or San Francisco or anywhere, they are going to tell you that we have too much SEC and we have too much FTC and we have too much ICC. There is not a bureau up here that they do not think we have too much of.

We appreciate the attitude that you all are taking about trying to restructure to get the Commission in line with the tax potential base that we have in this country. We are trying to reduce taxes.

Mr. WIRTH. Whatever that tax potential base is.

Mr. COLLINS. Well, whatever way we can keep taxes lower.

I want to ask about laws in other countries. Do you know of any country in the world that has as many restrictions and as much harassment on business as we impose to our own companies through the Foreign Corrupt Practices Act? Is there any other country in the entire world that harasses business like this one does?

Mr. SHAD. Not to my knowledge.

Mr. COLLINS. Not a one. This is the worst law in the world.

Mr. SHAD. I did not quite say that.

Mr. COLLINS. But you do not know of any that you would say is any worse?

Mr. SHAD. I do not know of any country that imposes prohibitions on bribery of foreign officials and accounting requirements as specific as those the Act provides.

Mr. FEDDERS. I agree with your statement.

Mr. WIRTH. Let's be careful about this. Isn't it true that every country has antibribery statutes?

Mr. SHAD. No, I do not believe that is true. I think that in many countries the statutes are mute as to bribery. You would think that every country might have such statutes. You would think that no one approves of bribery and certainly no one in the United States does.

Mr. WIRTH. We would certainly like to leave the record open for your submission on that front.

Mr. SHAD. Let me mention that was 1 of the 27 questions that we were asked to respond to on the 459 cases. And, of course, we could not do that; we do not have the resources to do that. There would be different responses for each country.

But you will see repeatedly in the information that we provided that it was unknown whether the conduct involved a violation of the local government's laws.

Mr. WIRTH. To glibly be talking about this is something that we do uniquely. Have we had our own Tanaka situation in this country? And the answer is no, right? And do we want to be getting ourselves into that? I think the answer is "no." I mean, let's not paint this with a simplistic kind of brush.

I think that the ambiguities that we have been talking about this morning in the attempt to define what it is we are doing is what we are after; not to say that because we happen to do this and maybe other countries do and maybe they do not, we do not want to walk ourselves into a Tanaka situation or a Lockheed situation or whatever.

I think that the political implications of what we are into in this country in terms of the nature of unfortunate practices and what we are trying to prevent——

Mr. COLLINS. Mr. Chairman, I want to be specific on this because I think it is a very important point, what other countries do.

When we trade with other countries, we are in the world market. As far as I know, other countries have domestic bribery laws, and they do not have foreign bribery laws. I do not know of any country that restricts foreign bribery. I would call on the chairman and I would call on any of you, and I would leave the record open if you know of any.

We see the biggest problem—in fact, the Chairman constantly keeps saying let's have hearings about foreign trade, let's have hearings about foreign trade. We are losing business to Japan, we are losing it to Germany, we are losing it to England, France, everybody. And one of the worst things is that we have come out with this law bill on foreign practices.

To what extent is a company liable for actions of its subsidiaries?

Mr. SHAD. Let me ask the general counsel to respond.

Mr. GREENE. With respect to the accounting provisions, the act talks solely about issuer. It does not mention subsidiaries at all. And the question is, Does the word "issuer" also include the issuer's subsidiaries on a consolidated basis or otherwise.

The Commission has taken the view that the act does include subsidiaries, but that is an ambiguous area. Is it all subsidiaries? Is it subsidiaries that are just controlled? The proposed legislation would try to make it clear that subsidiaries are covered but only if the issuer actually controls them.

Mr. COLLINS. How do you feel about decriminalizing the accounting provisions of the FCPA? Is there any need to have those criminal provisions regarding the accounting provisions?

Mr. GREENE. The Commission has not formally stated its view on that, but certain members of the staff I think personally would support decriminalization of the accounting provisions.

Mr. COLLINS. What about the requirements for liability for accounting violations by low- and mid-level officials? Do you think we need those provisions?

Mr. GREENE. There are no current provisions with respect to that. Again, it is an area of ambiguity as to what acts of low-level employees would bind a company.

The Commission's policy statement has suggested that if management did not know, and if there is a good system of controls, acts of low-level employees should not bind the company.

Mr. COLLINS. Mr. Chairman, right now, all of the enforcement action has involved knowing or reckless conduct rather than inadvertent violations. Is that the policy of the present Commission?

Mr. SHAD. Yes.

Mr. COLLINS. It is only on knowing or reckless violations?

Mr. SHAD. That is our policy statement, yes.

Mr. COLLINS. That is the way you do it. Have you had anyone at the Hill at any time ask you to do more?

Mr. SHAD. Do you mean go to—

Mr. COLLINS. Go back to inadvertent violations.

Mr. GREENE. Not that we are aware of.

Mr. COLLINS. So the administration encourages that, too. I think that is the current understanding of everyone in Washington today, and we would like to codify it.

Thank you, Mr. Chairman.

Mr. WIRTH. Going back to the earlier discussion, Mr. Shad, about, you know, what we do and what other countries do, it seems to me that there is a very dangerous lowest common denominator phenomenon that we could stoop to. The question that comes immediately to my mind, if you think U.S. companies ought to be permitted to bribe. Isn't that the logical consequence? Should they be permitted to bribe in order to be competitive?

Mr. SHAD. Well again, you alluded to the laws of other countries—an American company should not violate the laws in the countries where they do business.

Mr. WIRTH. But if the country does not have any law, if the American companies are dealing in some country that does not have those, should American companies be allowed to bribe there if there is no close country law related to that?

Mr. SHAD. Well, I am not an authority on business practices throughout the world. In some countries, the business practices are quite different than here. They are not considered in the area of what we would define as bribery.

My impression is it is less uncommon in some parts of the world, not universal by any means. But in some areas, my impression is that some of these questionable payments are a common business practice.

The act itself and our interpretations of it go well beyond "bribery." It is questionable payments. And a certain percentage of these questionable payments have been accomplished in other fashions.

One form would be where a purchaser of American equipment abroad would negotiate a very difficult contract in terms of the pricing of it, and finally once an agreement has been reached—say that the equipment is \$1 million—ask the American company to bill them \$1.2 million and put the extra \$200,000 in an account somewhere. It is circumvention of the local currency or exchange controls.

Mr. WIRTH. We have another vote and we will be right back. Thank you.

[Brief recess.]

Mr. WIRTH. The committee will come back to order. Mr. Shad, you said that the accounting provisions of FCPA are costly and burdensome.

Mr. SHAD. Could I briefly interject? I appreciate these breaks because I have the benefit of counsel. The comments that I made just prior to your departure were personal comments. You asked about bribery abroad. It is not an area that the Commission has, in fact, reacted to, and as the testimony indicates, we have only had two foreign bribery cases to deal with.

So I think that that is an area that is better addressed by the Justice Department that has had much more experience with that.

Mr. WIRTH. It does raise some interesting issues, since you have gone back to that.

We had a witness in our earlier hearing who was talking about—who has done a lot of studies for the Justice Department. He was stating very emphatically that we could not expect a corporation to operate under two different codes of conduct; one for its U.S. activities and one for its activities abroad.

He talked about what he called the contamination theory of corporate behavior, saying that corporate activities abroad could contaminate activities at home and could lead to a corporate mentality that encouraged illegal domestic activities. He just said a corporation cannot operate under two differing standards, and it seems to me that that is another window on the issue we are looking at. Do we want to try to define those lines carefully so that a corporation does not have to live in two different worlds, which they probably cannot do any more than you could or I could.

Mr. SHAD. Do you want me to react to that?

Mr. WIRTH. Sure.

Mr. SHAD. Again, we have indicated that we feel that the foreign bribery area should be consolidated within one agency. We are a disclosure agency, and apart from its disclosure aspects bribery is

not an area we have had a great deal of experience in. We are not comfortable in it in trying to be fully responsive to some of those nondisclosure related areas.

Our concern is disclosure.

Mr. WIRTH. I think the pattern shows—and Mr. Fedders might react to this—that most of the companies who were involved in improper illegal foreign payment situations were also involved in similar types of situations domestically with political contributions and commercial bribery and other activities here.

It would appear that there tends to be a flowing over from behavior domestically and behavior in a foreign country which would tend to support the testimony that was given us last summer.

Mr. FEDDERS. I would respectfully and cautiously disagree with that. From my own studies in reading the cases that were filed with regard to companies, I did not find that, if there were bribery problems overseas, there were necessarily problems domestically.

In many of the investigations I did for multinational corporations, there was no domestic problem whatsoever. They were solely international.

Sure, there were some that had domestic and foreign problems, but to say that it occurred in each and every case—

Mr. WIRTH. He is not suggesting that it occurred in each and every case. He says that as a pattern, it tends to occur more.

Mr. FEDDERS. I would not even say—and I did read all these cases that came out—I would not even say in the majority. It is not a study that has been done scientifically. I am operating on an impression. But I would not say even in the majority.

Mr. WIRTH. Well, going back to the question that we were discussing before the break, we are certainly not suggesting any condoning by you, Mr. Chairman, or the SEC—that we ought to say if there is not a foreign statute, that a company should be involved in bribery. That goes without saying, correct?

Mr. SHAD. Yes.

Mr. WIRTH. You said earlier in our discussion that the accounting provisions of FCPA are costly and burdensome, and that phrase has come up over and over and over again. Isn't it true, though, that a large portion of the costs incurred may be in the nature of one-time startup costs, such as those that many issuers incurred in conducting comprehensive reviews of their internal accounting control systems in taking corrective action with respect to deficiencies that they discovered?

Mr. SHAD. Well, there is a front-end cost in installing an internal control system, but there is a continuing cost, and again, uncertainty, under the present act as to the degree of detail.

The complaint that we have heard, and I am sure you have heard is concern over the possibility of being required to spend a million dollars to identify very small items. That is an ongoing cost; it is not just the installation of the control system.

Mr. WIRTH. What I just read was from the SEC response to the GAO report, where the SEC in March 1981 noted that the improved systems of internal accounting, what I just read was a quote from the SEC in which the SEC said that the improved costs of internal accounting should serve to reduce the cost of the annual audit of financial statements of issuers.

The SEC was saying, you know, a great part of this is that front-end cost. The question is, then, how much continuing cost and what do you pick up from that. But we all agree I think that there are a lot of set costs at the front for any accounting program, and a lot of this is picked up anyway. So let's not lay all the costs of setting up that accounting process on the FCPA, as the SEC has said.

Mr. SHAD. I think that in terms of the systems that have developed as a result of the FCPA, there were not only the front-end costs. There may be positive offsets in terms of better information being available to the auditors when they are certifying these statements, but I think that there is concern over continuing costs because of uncertainty and the degree of detail that industry has to go to to be sure that they are not in violation of the act.

Mr. WIRTH. Let's make it very clear that there are bookkeeping and recordkeeping requirements under other provisions of Federal securities' laws other than the accounting provisions of the Foreign Corrupt Practices Act, right?

Mr. SHAD. That is correct.

Mr. WIRTH. And nobody is suggesting that all of the bookkeeping and accounting provisions are required by FCPA, and therefore, this great burden is created by FCPA.

Mr. SHAD. It is the degree of detail that is the distinction.

Mr. WIRTH. Public companies have to disclose material information to investors?

Mr. SHAD. That is correct, but still, under the existing Securities Acts of 1933 and 1934, issues have to file accurate information with the Commission. The problem they find with the Foreign Corrupt Practices Act is that they have to have internal controls and accounts that will identify items that might not be subject to review and disclosure under the existing Securities Acts. It is the degree of detail.

Mr. WIRTH. Going to an earlier point that I want to make, while there is a degree of detail, as you are suggesting, all of the accounting requirements, the bookkeeping and recordkeeping, are not the result as some people have alleged, that we are having this huge burden because of FCPA. There are a whole variety of others as well.

In addition, the question was raised earlier today about criminal penalties for willful violation. Those criminal penalties, I think, Mr. Fedders, exist in other provisions of securities laws.

Mr. Fedders: That is correct.

Mr. WIRTH. For example?

Mr. FEDDERS. Section 32 provides the Department of Justice with the ability, if there is the necessary criminal nexus to violations of other provisions in the Federal securities laws, so you can have prosecution criminally of violations of section 10(b) on rule 10(b)-5 for example.

Mr. WIRTH. So the notion of criminal penalties is not new, either. It exists in the statute as well.

Mr. FEDDERS. It is not a new concept with regard to the Federal securities laws. It is a legislative determination, obviously, whether or not this kind of conduct should be criminalized where there is uncertainty, and I think that is the concern that Mr. Greene had in his mind when he expressed the view of some members of the

staff. This has not been decided at the Commission level. We would not personally object to the decriminalization of the provision.

The standards for imposing criminal liability on someone are obviously high. A criminal penalty is a far greater sanction than a civil penalty, and to impose a criminal penalty against someone for a law where there is this degree of uncertainty is quite difficult, and a burden that I am not sure should be undertaken.

Mr. WIRTH. We have a history of very strict law in the whole securities area. That is, there has been a very high standard and the expectation has been that people operating in the securities area will operate very carefully and will operate above the law.

For example, technically, violations of margin provisions are met with criminal penalties, or could be met with criminal penalties. That is what the law currently says. I mean, there is a high standard.

Mr. COLLINS. I have no further questions, Mr. Chairman.

Mr. RINALDO. I just want to thank Mr. Shad and the panel. I think they have been very helpful and they have targeted in on the problems with the act as it is presently constructed, and the difficulty that people have in arriving at a correct decision as to a proper course of conduct under the law.

Mr. SHAD. Thank you.

Mr. WIRTH. Just one final question, Mr. Shad. Going back to earlier discussions, you stated that in many cases it was impossible to tell whether a payment by a U.S. corporation violated a foreign country's law, but in both the Chafee and Rinaldo bills, and the bill reported out of the Senate Banking Committee, there is an exclusion under the bribery provisions for payments which are lawful in a foreign country.

If lawful is the standard and if, as you say, you cannot tell whether some payments are lawful, how can we provide certainty under the law with the proposed amendments?

Mr. SHAD. Well, if I said it was impossible, I did not intend to make it that strong. I believe I indicated that the response to the questions asked, was frequently unknown, that we did not know. But it was not a case where we had done an exhaustive analysis of the foreign country's laws to determine if the conduct in question was legal under foreign law.

I assume that if the provision is going to be to that effect, that would require issuers that wanted to engage in such payments to carefully research the laws of the countries involved so they would not be in violation. But we have not done that. We have not taken the more than 450 disclosures of questionable payments and researched the laws of all the different countries in which the questionable payments occurred. And, of course, not all of these disclosures involved foreign payments, either.

But we have not done an exhaustive analysis of foreign law.

Mr. WIRTH. Well, thank you very much. We greatly appreciate your time and effort, and in particular, the very good information which you provided to us earlier. We look forward to working with you on this, and I think your characterization, Mr. Fedders, of this being a discussion to try to hone this down and not an argument is absolutely correct, and that is what we are trying to get at. We need to ask where are those definitions and how do we do it.

I appreciate that attitude; I think it is very helpful. Also, I want to assure you that the chairman of the full committee and I are—we remain very concerned about the situation at the SEC in terms of the resources available there, and we look forward to having input from you when the warning bells go off, if they do.

Mr. SHAD. On behalf of us on the other side of the table, I would like to express our appreciation for the obvious enormous depth of inquiry to which the committee has gone, and the chairman in particular, and the lucidity of your inquiry. I think it is a compliment to your able staff and your own dedication to the problem.

Mr. WIRTH. Thank you. Some people accuse us of trying to figure out how many angels can dance on the head of a pin. Rather, we would like to go to the basic assumptions, go to the basic facts, and build from there rather than legislating by knee jerk in some fashion. Thank you very much.

Our second witness this morning, who has shown an extraordinary amount of patience and we are delighted to have with us, is Mr. Jonathan Rose, the Assistant Attorney General, Office of Legal Policy, the Department of Justice. And Mr. Rose will be talking with the subcommittee about the Department of Justice's enforcement of the Foreign Corrupt Practices Act.

And again, Mr. Rose, we would like to thank you and the Justice Department for your forthcoming nature in our inquiry and discussion of this legislation. You, as the SEC, have been the very helpful agencies in town, and we want to thank you and your staff. It is greatly appreciated that you put in that effort and you did respond. And if you run into your colleagues from the other departments we mentioned this morning, you might pass the word on that we are still looking forward to hearing from them.

Thank you, Mr. Rose.

STATEMENT OF JONATHAN C. ROSE, ASSISTANT ATTORNEY GENERAL, OFFICE OF LEGAL POLICY, DEPARTMENT OF JUSTICE

Mr. ROSE. We will certainly do that, Mr. Chairman.

Mr. Chairman, I am very pleased this morning to have the opportunity to appear before this subcommittee to participate in its oversight hearings on the Foreign Corrupt Practices Act.

You have asked me to describe the past and current enforcement efforts of the Department of Justice relating to bribery of foreign government officials by American companies. These efforts began more than a year before the enactment of the Foreign Corrupt Practices Act and have continued since December 1977 when that act was signed into law.

With your permission, I will describe our pre-FCPA cases as well as our enforcement actions under the Foreign Corrupt Practices Act itself.

As many of you will recall, it became public knowledge in the mid-1970's that a number of American corporations had engaged in possibly illegal practices involving domestic and foreign payments. I use the words "possibly illegal" advisedly because there was genuine uncertainty at the time over whether the foreign payments were, in fact, illegal.

In response to those revelations, the Securities and Exchange Commission developed a program under which publicly held corporations voluntarily made generic disclosures in public filings at the SEC of their past practices involving such overseas and domestic payments. In connection with this voluntary disclosure program, a substantial number of American corporations undertook internal investigations to determine the nature and extent of these practices.

In October 1976, the Department of Justice established its own task force to examine the facts underlying the voluntary corporate disclosures which had been made to the SEC in order to determine whether criminal statutes had been violated. At the time the task force was established, about 70 corporations made voluntary disclosures to the SEC about various payments made at home and abroad. By the summer of 1977, the number of corporations which had made voluntary disclosures to the SEC had risen to more than 400.

It soon became apparent that if the facts underlying the corporate disclosures were to be reviewed by the Justice Department prosecutors in a thorough and even-handed manner, the task force effort, as originally conceived, had to be expanded and intensified.

In the summer of 1977, 15 prosecutors were assigned full time to the task force. Special agents from the U.S. Customs Service, first 25 part time and later 7 full time, participated in the task force effort. In addition, the FBI was asked to conduct a survey of the relevant public filings.

Initially, the Department sought to identify those corporations whose activities warranted more thorough investigation. Eventually, the prosecutors assigned to the task force in Washington conducted investigations into disclosures made by approximately 90 companies. Various U.S. attorney's offices conducted investigations into disclosures made by another 140 companies. Since there have been substantial misconceptions about the nature of the voluntary disclosures that were made by these companies in the mid-1970's, it might be useful for me to take a moment to outline generally the results of the Department's review.

We found that relatively few of these corporations had actually disclosed to the SEC that their employees and officials had bribed foreign government officials. Apparently many corporations, acting upon the advice of counsel, disclosed any questionable practices they found, which practices in themselves might not have constituted either domestic or overseas bribery.

For example, approximately 25 corporations disclosed that they had been engaged in illegal ocean freight rebating. Publicly held ocean carriers had been engaged in the practice, in violation of the rate schedules regulated by the Federal Maritime Commission, of rebating to shippers a portion of the fees that the carrier charged for transporting the shipper's goods. This type of rebating had absolutely nothing to do with bribery of foreign officials; however, it led to the successful criminal prosecution of a number of carriers on the grounds that they had engaged in a criminal conspiracy to defraud the Federal Maritime Commission.

The Department's review also disclosed that many of the corporations which had made voluntary disclosures had engaged not in

bribery of foreign government officials, but rather, in a practice known as "accommodation overinvoicing." Corporations selling goods to foreign customers engaged in this practice in order to assist the customer in avoiding tax and currency control laws of the customer's home country.

To illustrate how far afield certain of these other disclosures were from the foreign bribery area, I would like to point to a few examples. Some of the larger liquor companies disclosed to the SEC that they had been making illegal rebates in the United States to domestic liquor distributors. The Department also learned that a number of corporations had declared possible violations of the Federal Elections Campaign Act which prohibited corporate contributions in Federal election campaigns.

The Department further discovered that a substantial number of companies disclosed as questionable payments commissions which had been paid to independent foreign sales agents. These commissions were often disclosed whenever the company had some indication that the commission appeared to be unusually large or was, for some other reason, possibly questionable. In many instances, there was no evidence that any portion of the commission had actually been passed on to a foreign government official.

The Department also discovered that certain companies had engaged in a practice of making payments to petty officials in connection with their performance of ministerial functions. The nature of these payments led the Department to conclude that investigations of this type of activity were not warranted. Similarly, in a number of other corporate disclosures, the amounts of payments were de minimis, and on that basis alone did not warrant further investigation.

Finally, the Department identified a number of companies which had paid bribes to foreign government officials. In the vast majority of instances, it was discovered that the payments had been made by overseas corporate subsidiaries without any territorial connection to the United States. Since no violation of Federal criminal law was found in those instances, the investigations were closed without prosecution.

In 10 instances, the Department was able to identify situations in which corporations had bribed foreign government officials, and in the process had violated an existing Federal criminal law. In those cases, the appropriate Federal criminal charges were filed.

Thus, the Department's review of the disclosures to the SEC made clear that far fewer than 400 companies had disclosed that they had engaged in the bribery of foreign government officials. In several instances, the Department brought public prosecutions against companies which had paid bribes to foreign government officials and in connection therewith had made false filings with an agency of the U.S. Government in violation of title 18 United States Code 1001. In other instances, the Department initiated prosecutions of corporations which, in the process of paying bribes to foreign government officials, had violated the Currency and Foreign Transactions Reporting Act. In several other instances, an extension of the so-called Isaacs-Kerner theory of mail fraud was utilized to prosecute companies for the act of bribery itself.

For the convenience of the subcommittee, I have attached to this statement a list of prosecutions resulting from the coordinated enforcement effort of the Department of Justice in this area. The list indicates which office brought the prosecution, the penalties paid by the defendants and the statutes under which the charges were brought. The pre-FCPA program has thus far resulted in the successful prosecution of six individuals and 18 corporations which have paid a total of \$7,662,000 in criminal fines, civil penalties, and civil settlements.

Mr. WIRTH. Mr. Rose, we have another vote, strengthening the District of Columbia I think. I will go over and vote and come right back. Thank you.

[Brief recess.]

Mr. WIRTH. Thank you, Mr. Rose. Why don't we resume.

Mr. ROSE. Mr. Chairman, the staff has indicated that it would be useful in the interest of time, which I know is running late, if I could summarize the rest of the statement which I am happy to do. I think copies of the full statement—

Mr. WIRTH. They will be included in the record in full and I thank you. I'm sorry; we have no control over what votes get called.

Mr. ROSE. Also, copies of the statement are available here and also at the Justice Department for people who want it.

I did want to make a point as to the statistics relating to our enforcement and some of the enforcement difficulties we have encountered in the postpassage period of the Foreign Corrupt Practices Act. We have completed 29 investigations which have led to two successful prosecutions. The facts of those prosecutions, summaries are included in the testimony. We are currently undertaking 57 investigations of allegations of violations of the Foreign Corrupt Practices Act.

The testimony also refers to a number of the difficulties that we have, given the peculiar nature of this statute. A very major one is that simple one of gathering evidence. This is a criminal statute. It requires proof beyond a reasonable doubt. To get proof from abroad, in many cases where governments and individuals have no particular motive, incentive, or desire to assist the United States in enforcement of this statute, is exceedingly difficult.

But the fact is, we have devoted a separate unit of the criminal division, the multinational frauds section, to the prosecution of these cases, and so long as it's on the books we plan to continue to do that.

The final thing that I wanted to say is that we have recognized that there is a legitimate and growing concern in the private sector and among many lawyers over what is perceived as a series of ambiguities in the language of the Foreign Corrupt Practices Act. We have established a Foreign Corrupt Practices Act business review procedure, which is very similar to the one we had in the antitrust division and still have.

When I was in the antitrust division, only a very few, I think a total of five transactions, have been reviewed under that procedure. So it doesn't seem to be a situation where we are attracting a fair amount of utilization of this process.

We are very concerned that this act be interpreted and enforced in a uniform manner. We think that in some respects the act is overbroad and confusing and unnecessarily uncertain and we think these problems ought to be corrected.

We also share with the Office of the Special Trade Representative and the Commerce and State and Treasury Departments a deep concern over the effect of the difficulties reported under the current law on trade competitiveness, as reflected in the Senate Committee Report on S. 708. We have reviewed these difficulties at the Cabinet level as an administration, and we believe that U.S. interests at home and abroad would be better served by the adoption of the administration-supported legislation along the lines of S. 708.

The Department believes that Congress can surely draft a law that is carefully designed to prescribe the conduct at issue. When any new law is passed, of course a period of experience with the law often reveals problems which the Congress must and generally does correct. In this area in particular, we believe that legislative reforms are imperative if we are to have an effective law prohibiting foreign bribery that does not result in unnecessary and unintended harm to our national economic interest.

In addition, inasmuch as our Nation is engaged in seeking an international solution to this problem of illicit payments, reform of the FCPA becomes more important in demonstrating to the world that it's possible to enforce a law of this kind without unnecessary harm to competitiveness.

I recognize the committee has not asked us here today to tell how the language of the existing law should be changed. We have been asked to report on the state of enforcement. We will honor the limits of that invitation, but we hope to have a return invitation very soon to explore with the committee ways in which the law might be improved.

The administration strongly supports, as I have already said, legislation along the lines of the Chafee-Rinaldo proposal, and would urge this subcommittee to take legislative action on this matter.

I would just add a couple of personal observations. This subcommittee I know is involved in undertaking work in a variety of extremely important fields. It's a very busy subcommittee. I know that. I know there's no political glory attached to trying to deal with this kind of problem particularly, or many of the other projects that this subcommittee is wrestling with.

The point that I would like to emphasize is that what we're dealing with here is a penal, not a civil regulatory statute. I think that often gets lost in the noise. People can get put in jail for this statute, and in our judgment it does represent a statute which is overly broad and has an in terrorem effect on all kinds of activities of a legitimate business nature that it was not intended to reach.

The chairman has discussed this morning the problem of anecdotal evidence. Well, you can only get so far by saying you need hard data. I am an antitrust lawyer by profession, and we have monopolization cases in the antitrust division and we have mountains of data, but ultimately you get down to the fact that liability—and courts do this every day—is based on witness after witness coming up with anecdotes. In the *AT&T* case, with which this committee is

very familiar, much of the evidence in that case is based on anecdotes of what AT&T has done to particular people.

So I don't think you can say that legislation can't be based on anecdotal evidence. It has to be based in part on anecdotal evidence and our own commonsense, which I do not think we can check at the committee door.

I would say that this is obviously not a partisan matter. President Carter and Special Trade Representative Askew pointed to the same problems we are pointing out, and I simply would hope that the committee, as I know it will, will approach this in a constructive way and try to look at the difficulties that we face as lawyers.

I know, Mr. Chairman, you are not a lawyer, but this is a very poorly drafted statute to reach the kind of conduct that it wants to reach. It is broad; it is vague. As a person who has advised a lot of people in private practice, I simply do not advise people to take risks with criminal statutes. It is extraordinary to me the kind of standard that we have here with this reason to know that the payment might be made—this is the kind of standard you typically find in food and drug laws, which deal with the public health of the citizens of the United States, not in this kind of a statute. So I would hope that the committee would look at that and carefully consider it.

[Testimony resumes on p. 204.]

[Mr. Rose's prepared statement follows:]

STATEMENT
OF
JONATHAN C. ROSE
ASSISTANT ATTORNEY GENERAL
OFFICE OF LEGAL POLICY
DEPARTMENT OF JUSTICE

Mr. Chairman, I am very pleased to have the opportunity to appear before the Subcommittee this morning to participate in its oversight hearings on the Foreign Corrupt Practices Act.

You have asked me to describe the past and current enforcement efforts of the Department of Justice relating to bribery of foreign government officials by American companies. These efforts began more than a year before the enactment of the Foreign Corrupt Practices Act (FCPA) and have continued since December 1977 when that Act was signed into law. With your permission, I will describe our pre-FCPA cases, as well as our enforcement actions under the Foreign Corrupt Practices Act itself.

I. THE DEPARTMENT OF JUSTICE'S INVESTIGATIONS WHICH PRE-DATED
THE ENACTMENT OF THE FOREIGN CORRUPT PRACTICES ACT

As many of you may recall, it became public knowledge in the mid-1970's that a number of American corporations had engaged in possibly illegal practices involving domestic and foreign payments. I use the words "possibly illegal" advisedly because there was genuine uncertainty at the time over whether the foreign payments were in fact illegal. In response to those revelations, the Securities and Exchange Commission developed a program under which publicly held corporations voluntarily made generic disclosures, in public filings at the Securities and Exchange Commission, of their past practices involving such overseas and domestic payments. In connection with this voluntary disclosures program, a substantial number of American

corporations undertook internal investigations to determine the nature and extent of these practices.

In October 1976, the Department of Justice established its own Task Force to examine the facts underlying the voluntary corporate disclosures which had been made to the Securities and Exchange Commission, in order to determine whether any criminal statutes had been violated. At the time the Task Force was established, about 70 corporations had made voluntary disclosures to the SEC about various payments made at home and abroad. By summer 1977, the number of corporations which had made voluntary disclosures had risen to more than 400. It soon became apparent that if the facts underlying the corporate disclosures were to be reviewed by Justice Department prosecutors in a thorough and even-handed manner, the Task Force effort, as originally conceived, had to be expanded and intensified.

In the summer of 1977, 15 prosecutors were assigned full-time to the Task Force. Special Agents from the United States Customs Service -- first 25 part-time and later 7 full-time -- participated in the Task Force effort. In addition, the Federal Bureau of Investigation was asked to conduct a survey of the relevant public filings. Initially, the Department sought to identify those corporations whose activities warranted more thorough investigation. Eventually the prosecutors assigned to the Task Force in Washington conducted investigations into disclosures made by approximately 90 corporations. Various United States Attorney's Offices conducted investigations into

disclosures made by another 140 corporations. Since there have been substantial misconceptions about the nature of the voluntary disclosures that were made by American corporations in the mid-1970's, it might be useful for me to take a moment to outline generally the results of the Department's review of those disclosures.

We found that relatively few of these corporations had actually disclosed to the Securities and Exchange Commission that their employees and officials had bribed foreign government officials. Apparently, many corporations, acting upon the advice of counsel, disclosed any questionable practices they found, which practices, in themselves, might not have constituted either domestic or overseas bribery. For example, approximately 25 corporations disclosed that they had been engaged in illegal ocean freight rebating. Publicly held ocean carriers had been engaged in the practice, in violation of the rate schedules regulated by the Federal Maritime Commission, of rebating to shippers a portion of the fees that the carrier charged for transporting the shippers' goods. This type of rebating had absolutely nothing to do with bribery of foreign officials. However, it led to the successful criminal prosecution of a number of carriers on the grounds that they had engaged in a criminal conspiracy to defraud the Federal Maritime Commission. These prosecutions were conducted by the United States Attorney's offices in Cleveland, Ohio and Newark, New Jersey.

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The Department's review also disclosed that many of the corporations which had made voluntary disclosures had engaged not in bribery of foreign government officials, but rather in a practice known as "accommodation overinvoicing". Corporations selling goods to foreign customers engaged in this practice in order to assist the customer in avoiding the tax and currency control laws of the customer's home country. For example, at the request of an overseas customer, a company would send an invoice for goods which indicated that the goods were worth \$120,000 when in fact the actual sales price for the goods had been \$100,000. The overseas customer would make a \$120,000 payment to the American corporation which would, in turn, remit the excess \$20,000 to the overseas customer's bank account either here in the United States or in some third country. In this way the overseas customer was able to maintain a U.S. dollar account which would be hidden from the authorities in his own country in violation of his country's currency control laws. The overseas customer would also thereby obtain documentation, in the form of falsely inflated invoices, to support a claim of increased costs which would reduce his tax liability in his own country. We found, in a number of instances, that the American companies which were supplying the inflated invoices would file Shipper's Export Declarations with the United States Customs Service and the Department of Commerce which reflected the higher invoice amount. Some of those cases were referred to the Department of Justice's Civil Division which brought civil actions against the

American companies enjoining them from the further filing of false Shipper's Export Declarations.

To illustrate how far afield certain of these disclosures were from the foreign bribery area, I would like to point to a few other examples. Some of the larger liquor companies disclosed to the Securities and Exchange Commission that they had been making illegal rebates in the United States to domestic liquor distributors. The Department also learned that a number of corporations had declared possible violations of the Federal Elections Campaign Act which prohibited corporate contributions in federal election campaigns.

The Department further discovered that a substantial number of companies disclosed, as "questionable" payments, commissions which had been paid to independent foreign sales agents. These commissions were often disclosed whenever the company had some indication that the commission appeared to be unusually large or was for some other reason possibly "questionable". In many such instances, there was no evidence that any portion of the commission had actually been passed on to a foreign government official.

The Department also discovered that certain companies had engaged in a practice of making payments to petty officials in connection with their performance of ministerial functions. The nature of these payments led the Department to conclude that investigations of this type of activity were not warranted.

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Similarly, in a number of corporate disclosures, the amounts of payments were de minimis and, on that basis alone, did not warrant further investigation.

Finally, the Department identified a limited number of companies which had paid bribes to foreign government officials. In the vast majority of instances, it was discovered that the payments had been made by overseas corporate subsidiaries without any territorial connection to the United States. Since no violations of federal criminal law were found, the investigations were closed without prosecution. In ten instances, the Department was able to identify situations in which corporations had bribed foreign government officials and in the process violated an existing federal criminal law. In those cases, the appropriate federal criminal charges were filed.

Thus, the Department's review of the disclosure to the Securities and Exchange Commission made clear that far fewer than 400 companies had disclosed that they had engaged in bribery of foreign government officials. In several instances, the Department brought public prosecutions against companies which had paid bribes to foreign government officials and in connection therewith had made false filings with an agency of the United States Government in violation of 18 U.S.C. §1001. In other instances, the Department initiated prosecutions of corporations which, in the process of paying bribes to foreign government officials, had violated the Currency and Foreign

Transactions Reporting Act.*/ In several instances, an extension of the so-called Isaacs-Kerner theory of mail fraud was utilized to prosecute companies for the act of bribery itself. See United States v. Isaacs, 493 F.2d 1124 (7th Cir. 1974). Under that theory, a person paying a bribe to a government official can be prosecuted under the mail fraud statute on the ground that he engaged in a scheme to defraud the public, or the employing government, of the honest services of the recipient of the bribe, in violation of the recipient's fiduciary duty.

For the convenience of the Subcommittee, I have attached to this statement a list of the prosecutions resulting from the coordinated enforcement efforts of the Department of Justice in this area. The list indicates the office which brought the prosecution, the penalties paid by the defendants and the statutes under which the charges were brought. The pre-FCPA program has thus far resulted in the successful prosecution of six individuals and eighteen corporations which have paid a total of \$7,662,000 in criminal fines, civil penalties and civil settlements.

*/ The Currency and Foreign Transactions Reporting Act makes it an offense for anyone to transport into or out of the United States \$5,000 or more in currency or bearer instruments without reporting certain information to the United States Customs Service.

II. THE DEPARTMENT OF JUSTICE'S ENFORCEMENT PROGRAM
UNDER THE FOREIGN CORRUPT PRACTICES ACT

The pre-FCPA enforcement effort, which as I stated began in the summer of 1977, is only now being completed. With the enactment of the Foreign Corrupt Practices Act in December 1977, the same group of prosecutors responsible for investigating and prosecuting pre-FCPA violations were also charged with the responsibility for investigating and prosecuting violations of the new statute. Because of the highly sensitive nature of these cases arising from their potential foreign policy and national security implications, the United States Attorney's manual has been amended so that most of the Foreign Corrupt Practices Act investigations are being conducted by Justice Department prosecutors in the Fraud Section of the Criminal Division here in Washington rather than by the various United States Attorneys' offices. Investigations are conducted here in Washington to maintain close supervision of these cases and to minimize the adverse foreign policy consequences that any one of these cases can produce.

Thus far, the Department has completed 29 investigations into allegations of violation of the Foreign Corrupt Practices Act. These completed investigations have led to two public prosecutions by the Department of Justice. The first such prosecution was a civil injunctive action in United States v. Roy J. Carver, et al. In that case, Mr. Carver had disclosed to the United States Ambassador to Qatar that he and his associate had

obtained an oil concession in Qatar, prior to the effective date of the Foreign Corrupt Practices Act, by paying a \$1.5 million bribe to Qatar's Director of Petroleum. After the Act became effective, Mr. Carver and his associate sought the assistance of the Ambassador in identifying an official of Qatar who could be paid to renew the concession. Our enforcement action resulted in the defendants being enjoined from future violation of the Act.

The second public prosecution by the Department of Justice under the Foreign Corrupt Practices Act was brought against the Kenny International Corp. and its owner Finbar B. Kenny. In that case, the defendants had paid \$337,000 to the Prime Minister of the Cook Islands. The payment took the form of a contribution to the political party of the Prime Minister in return for an agreement from the Prime Minister that if re-elected he would renew an exclusive stamp distribution contract which Mr. Kenny had with the Cook Islands government. The corporation pled guilty to a criminal violation of the Foreign Corrupt Practices Act and paid criminal fines of \$50,000. Both Mr. Kenny and the corporation consented to a civil injunction under the Act and made restitution of \$337,000 to the Cook Islands Government.

The Department of Justice is currently conducting approximately 57 investigations of allegations of Foreign Corrupt Practices Act violations. Some of these investigations have continued for as long as three years. Many are difficult and complex. As is often the case in white collar crime

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investigations, the Department, in some instances, has had to review hundreds of thousands of documents, interview dozens of witnesses and adduce testimony before the Grand Jury from dozens more.

Added to the difficulties of ordinary complex investigations are some considerations unique to the Foreign Corrupt Practices Act which the Department has come to understand better as it has gained enforcement experience under the Act. It may be useful to share with you some of these considerations.

In an ordinary domestic bribery case, the offense is usually committed by two parties, i.e., the citizen who pays the bribe and the public official who receives the bribe. Since ordinarily neither of these two parties is willing to testify voluntarily about the transaction, a standard approach used by prosecutors to investigate domestic bribery is to offer one of the two consenting parties immunity or a favorable plea agreement in return for testimony against the other party. Generally, the government offers such a favorable disposition to the citizen who paid the bribe on the theory that there is a greater public interest in successfully prosecuting and removing from office the corrupt public official than there is in pursuing the person who paid the bribe.

The Foreign Corrupt Practices Act is, however, a bribery statute which is quite different from domestic bribery laws. The Congress clearly intended that prosecution of the corrupt foreign official be left to his or her own government.

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Under the Foreign Corrupt Practices Act, therefore, only the conduct of the United States citizen or entity paying the bribe is criminalized. For obvious reasons, we cannot and have not attempted to obtain the testimony of the corrupt foreign official who has received the bribe for use against the Americans who may have made the payment. Thus, in order to prosecute American companies or citizens for violation of the Foreign Corrupt Practices Act we have had to develop evidence of the violation without the cooperation of either the offeror or the recipient of the bribe.

Another investigative limitation which results from the nature of the Foreign Corrupt Practices Act is that the Department has been unable to utilize some of the more traditional international evidence gathering tools, such as Interpol. Interpol, as you know, functions through local foreign law enforcement agencies. When our law enforcement authorities make a request for assistance through Interpol, local law enforcement agencies in the foreign country conduct the investigation. Because allegations of violation of the Foreign Corrupt Practices Act often involve allegations of corrupt payments to senior foreign government officials, we have been of the view that it would usually be inappropriate to ask foreign law enforcement agencies to conduct investigations on our behalf into the activities of their own government officials.

Still another limitation on how we conduct investigations of Foreign Corrupt Practices Act violations is imposed by

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a peculiar feature of bribery cases. Our experience has shown that all too often criminal confidence men operating as middlemen overseas, in order to induce their victims to part with their money in a transnational transaction, will suggest to the victim that extra money is essential in order to bribe a foreign government official. Although he may even identify the foreign government official, the confidence man may have no intention of bribing that government official and that government official may have no knowledge of the confidence man's representations to the victim. This situation can occur, not only when an independent operator attempts to defraud his victim, but also when a renegade employee attempts to defraud his own employer and embezzle the money.

Finally, soon after the enactment of the Foreign Corrupt Practices Act, the Department recognized that there was a growing and legitimate concern in the private sector and among many lawyers over what were perceived as ambiguities in language in the Foreign Corrupt Practices Act. In response, the Department established the Foreign Corrupt Practices Act Review Procedure, which is modeled after the Antitrust Division's Business Review Procedure, under which a company can submit for the Department's review a written description of a proposed transnational commercial transaction. After reviewing the transaction, the Department will inform the company whether or

not it will take any enforcement action under the FCPA if the transaction proceeds.

The Department had hoped that the establishment of the Review Procedure program would provide a mechanism which would eliminate doubts about the meaning and application of the Foreign Corrupt Practices Act and thereby prevent any unnecessary losses of exports due to perceived uncertainty about the Act. Unfortunately, relatively few companies have taken advantage of the Procedure. Thus far, the Department has published only four releases describing our actions under the Procedure. Three additional requests are pending. In part, we believe this underutilization of the review procedure results from a concern that confidential business information provided to the Department of Justice as part of the program would ultimately be publicly disclosed under the Freedom of Information Act.

The Department of Justice is very concerned that the Act be interpreted and enforced in a predictable and uniform manner. Our concern stems from what we believe are problems with the existing Act's clarity. We believe that in some respects the Act is overly broad, sometimes confusing, and often unnecessarily uncertain in its application. These problems ought to be corrected. We also share with the Office of the Special Trade Representative, the Department of Commerce, the Department of State, and the Treasury Department a deep concern over the effect of the difficulties reported under the current law on trade competitiveness.

This Administration has carefully and thoroughly reviewed the difficulties encountered under the Foreign Corrupt Practices Act at the Cabinet-level, with involvement by all interested agencies, and has agreed upon specific legislative reforms. We believe that U.S. interests at home and abroad would be better served by the adoption of the Administration supported reform legislation.

The Department believes that surely the Congress can draft a law that is carefully designed to proscribe the conduct at issue. When any new law is passed, a period of experience with the law often reveals problems which the Congress must and generally does correct.

In this area, in particular, we believe that legislative reforms are imperative if we are to have an effective law prohibiting foreign bribery that does not result in unnecessary and unintended harm to our national economic interests. In addition, in as much as our nation is engaged in seeking an international solution to the problem of illicit payments, reform of the FCPA becomes that much more important in demonstrating to the world that it is possible to enforce a law of this kind without unnecessary harm to competitiveness.

I recognize, however, that the Committee has not invited testimony on how the language of the existing law should be changed. Rather, we have been asked here today to report on

how the existing law is being enforced. We will honor the limits of that invitation and not take up the Committee's time with a set of recommendations which we believe deserve full and separate consideration. We would hope to have a return invitation very soon to explore with the Committee ways in which the law should be improved. As you know, the Senate has already recognized the need for change and has undertaken some very useful steps in this area. The Administration strongly supports legislation along the lines of the Chafee-Rinaldo proposal, and urges this Subcommittee to take legislative action on this matter.

I would be pleased to answer any questions the Subcommittee may have.

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DISPOSITION OF IMPROPER OVERSEAS PAYMENT CASES (PRE-FOREIGN CORRUPT PRACTICES ACT CASES)

<u>DATE</u>	<u>PROSECUTION</u>	<u>DEFENDANT</u>	<u>PENALTIES*</u>	<u>CHARGE</u>
3/16/78 (plea) 10/23/78 (sentence)	USA-N.D. Ohio	Seatrain Lines, Inc. and Ocean Equipment Corporation	\$ 260,000 \$ 260,000	18 U.S.C. 371 31 U.S.C. 1059 31 U.S.C. 1101(a)
3/16/78 (plea) 5/1/78 (sentence)	USA-N.D. Ohio	Harvey Ludwig	\$ 10,000	18 U.S.C. 371
3/24/78 date plea filed	DOJ, Fraud Section	The Williams Companies	\$ 198,000	18 U.S.C. 1343 31 U.S.C. 1059
4/11/78 date plea filed	USA-N.J.	Sea-Land Service, Inc.	\$ 5,000	18 U.S.C. 371
4/26/78 date plea filed	DOJ, Fraud Section	Control Data Corp.	\$ 1,381,000	18 U.S.C. 1343 31 U.S.C. 1059
5/10/78 date of plea and sentence	USA-N.J.	United States Lines, Inc.	\$ 5,000	18 U.S.C. 371
7/19/78 filing of information	USA-S.D.N.Y.	United Brands Company	\$ 15,000	18 U.S.C. 1343 18 U.S.C. 371
11/20/78 date plea filed	DOJ, Fraud Section	Westinghouse Electric Corporation	\$ 300,000	18 U.S.C. 1001
1/3/79 date plea filed	DOJ, Fraud Section	Gulfstream American Corporation (formerly Grumman American Aviation Corporation)	\$ 120,000	18 U.S.C. 1001

* Penalties include criminal fines, civil penalties, and civil settlements.

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Mr. WIRTH. Thank you very much. I really want to go to some questions about language. I appreciate that and you are quite correct in noting that a number of the agendas in front of the subcommittee are extremely important in terms of public policy but very difficult to explain to constituents.

As you can see, you say to people what have you been doing and you say, well, I have been rewriting the Communications Act. People look at you and wonder what else you have been doing. Working on the Foreign Corrupt Practices Act. Yes?

Well, let us walk through, if we can. Let me ask you a similar question that I asked Chairman Shad, related to the activities of the Justice Department under the Foreign Corrupt Practices Act. You have brought two cases in 4 years under the Foreign Corrupt Practices Act. Does that suggest to us that the act has been successful in preventing foreign bribery?

Mr. ROSE. I don't think it suggests very much, Mr. Chairman, beyond the fact—we have 57 current investigations going on, which is quite a large number. I think it does speak to the fact that this is a criminal statute. As the Justice Department, we don't indict simply on probable cause, which is the standard that the grand jury must find when it indicts someone. We indict someone when we think we have the evidence in hand to convict that person by proving to a petty jury in a criminal trial that that person is guilty or that company is guilty of a violation of a statute beyond a reasonable doubt.

That is a very heavy burden that the Government undertakes in a criminal case, and it is very difficult, when you are dealing with foreign governments. I really speak to this more from my experience as an antitrust lawyer, but it is the same problem of evidence gathering from foreigners in particular.

Here we have a situation in this statute where you have two countries involved, two people involved, and typically the foreign country, unlike a commercial bribery situation in the United States, which Federal law also prohibits, there is no incentive for the foreigners to cooperate with our prosecutions under this statute. To the extent they do it, it is a matter of grace. You are constantly met with resistance from the foreign policy bureaucracies in these countries.

Evidence gathering in these areas is exceedingly difficult and I have enormous sympathy with the people that are actually on the firing line trying to bring these cases.

Mr. WIRTH. You have closed 27 cases without prosecution?

Mr. ROSE. That is correct, sir.

Mr. WIRTH. A summary of those is attached to your testimony?

Mr. ROSE. A summary of the closed cases is not. We summarize the cases where we have brought an indictment. Here again, we are dealing with cases which are results of grand jury investigations. There are the normal rules of grand jury secrecy. It is not in our view fair or proper law enforcement practice when one closes an investigation then to make public or to share in a way that might be made public the results of an investigation where no prosecution was brought.

Mr. WIRTH. All those 27 were looked at by the grand jury?

Mr. ROSE. I believe that is correct; yes, sir.

Mr. WIRTH. And the 57 current investigations are all in front of the grand jury; is that right?

Mr. ROSE. I believe that is correct, yes, sir. It may involve a few preliminary ones, but I do not think so. Most of those are before a grand jury.

Mr. WIRTH. Do you have any prediction as to what is going to happen to those 57 cases? Do you have any feel for that?

Mr. ROSE. No because again, we are simply faced with a prosecutorial decision under a criminal statute that has to be made being satisfied that you can meet the burden of beyond a reasonable doubt in terms of bringing the case. Except where we have actually concluded to bring an indictment, I would certainly not be confident as a prosecutor to predict whether I will bring one or not until I have had a chance to review all the evidence, and in those 57 the investigations are not complete yet.

Mr. WIRTH. So there is no way of projecting what might happen out of those 57?

Mr. ROSE. No, sir. I should note, by the way, that those are, I think, the vast majority, with the exception of two or three, are pre-FCPA cases, again.

Mr. WIRTH. On that front, on page 4 of the submission of the Justice Department, the Department said that some pre-Foreign Corrupt Practices Act cases that came before the enactment of the FCPA were closed before the investigations were completed because of limited manpower. That is what the Justice Department told us.

Do you know when those cases were closed and how many cases fell into this category?

Mr. ROSE. I am sure that they were all in the last administration. I think we got clearly adequate manpower to carry out the open investigations we have now. Of course you also, I think in a number of those cases, would have statute of limitations problems because when you are talking about pre-1977 behavior and a 5-year statute of limitations, you can figure out that something that happened prior to 5 years ago simply could not be brought because of the statute.

Mr. WIRTH. You were suggesting earlier limited manpower in the Justice Department was responsible for prosecuting cases under FCPA. How many people do you have now in the Justice Department?

Mr. ROSE. I believe we have eight prosecutors working on it full time. It is a separate section of the criminal division. I am not aware of manpower problems. Now, I am not going to make confident predictions about future budget actions. As you say, we are involved in quite an exercise this week. So I am not going to talk about what may be done to our budget in the future, but that is perfectly adequate manpower to handle this problem, we think.

Mr. WIRTH. You were saying that you attempted to consolidate enforcement of this?

Mr. ROSE. Within the multinational frauds section of the Criminal Division, for a couple of reasons. These cases, as I have indicated, where you have problems of gathering evidence which has to be made available from foreign countries, either from private citizens there or from foreign governments, we often need to use the good

offices of the State Department. It is not a very functionally effective way to deal with these cases to have them scattered throughout 94 U.S. attorney's offices. We simply have to deal with foreign governments through the established diplomatic channels, and that is much easier to do from Washington than from a U.S. attorney's office in the field.

Mr. WIRTH. You say the eight people are adequate to do the job? Do you think there could be—

Mr. ROSE. I am not saying that we just have eight people. I believe it is eight full-time prosecutors, which are lawyers. Obviously, they are supported by a larger staff than that.

Mr. WIRTH. And that does not, a small group like that does not suggest that there is very little possibility of detection?

Mr. ROSE. No, I do not think that is the issue of a very little possibility of detection. We have a situation where we have been able to—of course, obviously, we do not send roving investigators.

That is one of the interesting things about this statute.

Mr. WIRTH. I am trying to get a feel for what your perception of the statute is and how it is enforced.

Mr. ROSE. Well, I am very interested in it because you know, we would all oppose murders being committed abroad but we do not have any statute which forbids that, and we obviously do not have roving investigators going to every foreign country with whom we trade abroad trying to find out whether there is a case of foreign bribery.

This is quite an extension extraterritorially of our criminal law, and to the extent we are able to deal with disclosures and evidence turns up, we think this is a perfectly adequate prosecutorial force.

But this is a very unusual law, and as I point out, a very ill-drafted law, and really is in need of drafting attention, just for pure competence. You say you are going to ask me about that later, so I will reserve my comments.

Mr. WIRTH. If all of the jurisdiction of the various agencies were collected in the Justice Department for prosecuting foreign bribery cases, would this require that you beef up the multinational fraud unit?

Mr. ROSE. I am not sure that it would extensively, but we are the only agency, I think, that has a separate section devoted to this problem. I am not intimately familiar with the organization of the SEC, but I do not believe they have any specific, other than the general enforcement section, any specific unit devoted to the enforcement of this law.

We do, and of course if enforcement were consolidated in our jurisdiction, we would have such a unit and would give it adequate people so that the law could be fully enforced.

I think we have displayed over the years since the statute was passed a sincere commitment to do the best we can with what is an exceedingly poorly drafted statute.

Mr. WIRTH. Let me jump into some of the drafting questions. You said a couple of times here that the language is in need of redrafting and is confusing and is often unnecessarily uncertain. I believe those are words that you used.

Mr. ROSE. A direct quote, I think.

Mr. WIRTH. On page 15 of your statement you say that the Senate has undertaken some very useful steps in changing the act. Let me read a few items from the bill reported out of the Senate Banking Committee and see if you think this is well-drafted language.

The committee print on page 27 under section 104(C)—

Mr. ROSE. I am afraid I will have to get with you, Mr. Chairman, because it is impossible to play by ear on one of these things.

Mr. WIRTH. We all play by ear on a steady basis, Mr. Rose.

Mr. ROSE. I know you do up here, but I try not to.

Mr. WIRTH. Page 27, under section 204(C), subsections A and B, the antibribery provisions, shall not apply to "any expenditures, including travel and lodging and expenses associated with the selling or purchasing of goods and services or with the demonstration or explanation of a product."

How in the world would you ever convict somebody, it seems to me, even if they paid \$1 million bribe to the president of some country, to win a multimillion dollar contract, if all that person had to do was to claim that the bribe was merely an expenditure associated with selling goods and services. That is pretty ambiguous in itself, isn't it?

Mr. ROSE. I think that particular section is a well-intentioned section trying to get at—

Mr. WIRTH. The whole bill is well-intentioned.

Mr. ROSE. So is the bill—I could read back to you, and I would be glad to do it, sections from the current law that is on the books that we are enforcing criminally, and it is equally hopeless in its attempt at interpretation.

I think what we have here is a situation—really, it is. If you look at what does "corruptly" mean? Then there is a long legislative history that goes through that "corruptly" means it does not cover facilitating payments and grease payments and things of that nature.

I as a prosecutor am supposed to attempt to deal with that in a criminal court. That is a law that is on the books. This is simply a reported bill.

Now I will agree that this business of—I think what they are attempting to get at here is a very significant problem, which is the difficulty of customary payments abroad, so-called grease or facilitating payments, where you are dealing with people who refuse to do that which they ought to do without some kind of tip or gratuity.

That is obviously not something we are familiar with in the United States. Our businesses don't do it. It is unfortunately a reality abroad and I think this language has attempted to try to deal with what is equally hopeless language in the act that is on the books. While I agree with you that this may not be the best stab at it, I think it is vital that we take some stab at it.

Mr. WIRTH. I was just pointing out that I still do not think we have a product.

Mr. ROSE. Right.

Mr. WIRTH. If you read on in No. 5, it says, "any ordinary expenditures, including travel and lodging expenses associated with the performance of a contract with a foreign government or agency

thereof". What is an ordinary expenditure? That is again presenting the same kind of problem and I just wanted to raise those two to pick up on your offer.

Mr. ROSE. We are certainly prepared to work with this committee to draft a statute that will work. We have absolutely no problem with that and we certainly hope we will have the opportunity to do that. I agree with you that these two exceptions are fairly broadly drafted, but the language in the current law is equally difficult, it seems to me, and that is one of the problems that we have of bringing successful criminal prosecutions.

Mr. WIRTH. Let me read another one. Section 104 states that the bribery prohibitions will not apply to "any payment, gift, offer or promise of anything of value which constitutes a courtesy, a token of regard or esteem or in return for hospitality".

Mr. ROSE. Well again, I think that all of these sections are devoted to a very significant problem, which is here we have, and I can tell you from personal experience in negotiating with foreigners, an attempt to get a multilateral agreement on something that will prohibit the core kind of conduct that Congress is trying to get at here. The foreigners love our law. They think it is wonderfully broad and ambiguous and impairs our companies and they think it is just fine that we have one and they are glad—they are not planning to enter into any multinational agreement on it because they know the reality of dealing in the Middle East and a lot of other parts of the world is that people simply do not function as we do in the United States and simply expect and demand some kinds of payments in order to perform their functions, which they ought to perform.

Mr. WIRTH. We understand that is what is said about the act.

Mr. ROSE. I hope you do, OK.

Mr. WIRTH. The diamonds given by Bokassa to Valery Giscard d'Estaing would have qualified, I think, under courtesy, token of regard or esteem.

Mr. ROSE. I doubt that.

Mr. WIRTH. Mr. Rinaldo.

Mr. RINALDO. Thank you, Mr. Chairman.

You know, it is interesting that the chairman points out what we might call ambiguities. There are plenty of ambiguities in the present language of the FPCA.

Mr. WIRTH. We have been talking about that.

Mr. RINALDO. Perhaps maybe we can even improve on the Senate bill and maybe that should be our objective here.

Let me ask you a key question. Do you feel that the statute, as written, has the clarity and specificity that should be required of a criminal statute?

Mr. ROSE. No, Mr. Rinaldo, I really do not. I do not think it is responsible legislation, and this is why I differentiate very clearly because the Congress quite often, and I understand it, although those of us charged with implementing laws do not particularly appreciate it, gives an executive branch or an independent regulatory agency a broad civil regulatory mandate to control certain kinds of conduct and then says we will have oversight in order to make sure you carry out the statute in the way that we intended it.

With a penal criminal law, this is simply not a possible approach. Maybe I could just take this opportunity to read the language of the current law. I will not read the whole thing because it is a very long statute, to start with, for a criminal law; it goes on for pages. The basic point here is that it "shall be unlawful for any issuer, namely subject to the jurisdiction of the SEC, to make use of the mails in furtherance of an offer to give any foreign official, for the purposes of influencing any act or inducing any foreign official to use his influence in order to assist such issuer to obtain business".

It says "any person". Now this is the individual liability which is so destructive to I think business conduct, and I particularly found this in the private sector. Businessmen simply do not go anywhere near conduct if they are trying to run a proper business that could stimulate a grand jury investigation. That is why when you talk about "any person, while knowing or having reason to know that all or any portion of such money or thing of value will be offered directly or indirectly to any foreign official" violates the criminal law, well, this "knowing or having reason to know" and "corruptly" language is the poorest kind of drafting possible in terms of a criminal statute.

Now if this were a civil statute, I would feel very differently about it, and it is in part civil. But that is not our part of it. That is the SEC's part of it under current law. This is what is really troubling us and I think the chairman has pointed out quite appropriately that in the Senate bill there are perhaps possible better ways of doing what is sought to be achieved, namely making this a precise, enforceable criminal statute. And I would hope that this committee could work on that and try to improve it and we certainly stand ready with the committee to do that.

Mr. RINALDO. I have a few more questions, but we have a vote on. I will be right back and I can ask you then.

[Brief recess.]

Mr. ROSE. Mr. Chairman, could I clean something up?

Mr. WIRTH. Please do. Let us clean up the record.

Mr. ROSE. That is one of the benefits, as Chairman Shad mentioned before.

The first point I should make is that the number of prosecutors—you asked about the number of full-time people in our multinational fraud unit of the criminal division. That has ranged from a minimum of 8 up to 10 and we have more available if there are reasons to have that. And we indeed have some of our criminal division working—

Mr. WIRTH. These are lawyers?

Mr. ROSE. These are lawyers, yes. These are lawyers.

Mr. WIRTH. As a nonlawyer, I wanted to make that distinction.

Mr. ROSE. Fair enough.

The second point is that the 57 ongoing investigations we have, I misspoke. They are post-Foreign Corrupt Practices Act cases, which are investigations ongoing under the act.

Third, you asked about possible need for additional resources—and I do not have that readily available; I am going to get back to you on that—if the jurisdiction were consolidated. We did provide,

as required, to the Senate Banking Committee an estimate of what additional resources would be required.

My last point would simply be that, with regard to the core prohibition of the statute, I expect that it would not be justified for some defense lawyer to claim that, in cases of obvious violation of this statute, that the prohibition is too vague so that a prosecution should not lie. That simply is not the case.

What I am dealing with here is simply the problem of the broad reach of a criminal statute which is in certain of its aspects vague, prohibiting conduct, not reaching conduct, and affecting conduct by companies who simply do not want to run afoul of a penal prohibition and thereby forego export opportunities or opportunities to engage in business abroad just so they will not be involved with this particular statute.

And I think you pointed out quite properly that there is some vagueness in the attempt in the Senate to deal with certain of the problems which were attempted to be dealt with by the House committee last time in terms of these facilitating payments. The provisions in the Senate bill are not entirely satisfactory to us either and we are prepared to work with you to resolve the ambiguities.

The House-passed bill and the bill that is now the law, though, attempted to deal with the same situation by the use of the word "corruptly" and then providing legislative history saying that when we used the word "corruptly" we did not mean to cover facilitating or grease payments. And they also put into the definition of "foreign official" that it does not include a ministerial or clerical level official.

But the difficulty is, I think, there that that is in and of itself a pretty weak reed for someone to lean on in advising a client. So the problem is that we are trying to see us have a law on the books that somebody can advise a client safely that he can do certain things in the conduct of his business abroad without running into possible violation of a penal statute. That was the basic point I was trying to make.

Mr. WIRTH. Following up on that, assuming that legislation passes in the Senate—it has been a roller-coaster over there in terms of the initial legislation, and then a change, and then a change, and now I understand there are changes going to the floor from the Commerce Committee. So far there is not fine agreement on that, as some have alleged that there has been.

But after that passes, can we make this point, and assuming that it does, can we make a formal request of the Justice Department for your reaction to that language? I cited some of the ambiguities in the current language that may be changed between now and the floor. But you all are the people on the firing line on this and you know, you understand what is possible and what is not possible, or your interpretation of what is and is not possible.

And we would like to, if we might, make a formal request of you to get your reaction to that language after it passes. Can we do that formally right now?

Mr. ROSE. Yes, sir. We would be fully prepared to do that.

Mr. WIRTH. Terrific.

Let me ask another question while we are waiting for Mr. Rinaldo. Under the current law, a corporation or an individual can be

guilty of violating the Foreign Corrupt Practices Act if that corporation or individual makes a payment to a foreign official to influence his act or decision, or if payment is made to any person while "knowing or having reason to know," that the payment will be passed on.

The purpose of that, looking back into the history of the legislation here, the purpose of that was to reach acts of foreign agents, which was a primary means of making foreign bribes.

Mr. ROSE. Right.

Mr. WIRTH. The Chafee-Rinaldo proposal would change the reason to know standard to direct or authorize. In other words, reason to know is not enough; it would have to be directed or authorized. Thus, unless a corporate official actually directed an agent to bribe he would not violate the Foreign Corrupt Practices Act.

Now, that is a shift being made within the legislation, correct?

Mr. ROSE. I think that is right. But I think they also put, in order to cover what would be a knowledgeable but kind of winking agreement, "pattern of conduct," I believe is also included in the Senate version. So it would either be direct or authorize directly or by a pattern or course of conduct, I believe is the language as I last saw it.

Mr. WIRTH. Now, the question focuses here on agents. The Department of Justice submission that you sent to us, most of the instances cited in that submission involve situations where funds that were used to make foreign payments were accumulated through the use of agents and were paid to foreign government officials through agents or brokers.

How in that situation under the changed language would the Department of Justice prove a corporation's responsibility?

Mr. ROSE. Well, I think what the effort is is to try to draw a line between the conduct if a corporation directly authorizes, directs or authorizes or through a pattern or course of conduct, which I assume would include aid to foreign agents, where you had a situation of clear knowledge that this was intended to be, the use of an agent was simply intended to be a cloak for a direct payment, that they were either directing or authorizing or by a course of conduct authorizing.

Impliedly, we would be able to reach that conduct. I think it is this outer limit that has so troubled people in dealing with the law as it now stands, because the use of middlemen or agents in some countries is very customary, and the difficulty of being able to control their conduct and whether indeed a criminal law of the United States, which as I pointed out earlier was exceptional in its extra-territorial application anyway, should try to reach conduct of foreign nationals operating in their own jurisdiction, is I think one of the questions that really is one that should be looked at very carefully.

At least if we are going to make that penal, it ought to be a very clear kind of prohibition, as opposed to civil. As I say, I think this criminal versus civil distinction is a very important one that tends to get lost in the debate.

Mr. WIRTH. But how do you avoid the winking, to use your phrase? They know what is going on but they have not directly au-

<u>DATE</u>	<u>PROSECUTION</u>	<u>DEFENDANT</u>	<u>PENALTIES*</u>	<u>CHARGE</u>
6/1/79 date plea filed	DOJ, Fraud Section	Lockheed Aircraft Corporation	\$ 647,000	18 U.S.C. 1343 18 U.S.C. 1001 31 U.S.C. 1058
6/4/79 date plea filed	DOJ, Fraud Section	Page Airways, Inc.	\$ 52,647	31 U.S.C. 1058
6/10/79 date plea filed	DOJ, Fraud Section	Textron, Inc.	\$ 131,670	31 U.S.C. 1059
7/24/80 date information filed	USA-S.D.N.Y.	Bethlehem Steel Corporation	\$ 325,000	18 U.S.C. 371, 1341, 1343 31 U.S.C. 1059, 1101(a)
10/28/80 date of judgment	USA-S.D.N.Y.	Thomas Lamonica	\$ 1,000 2 yrs. probation	18 U.S.C. 1343, 1341
9/79	E.D. Penn- sylvania	Joseph E. Seagram & Sons, Inc.	\$1,500,724	27 U.S.C. 205(c) 31 U.S.C. 1058
2/22/78	E.D. Louisiana	J. Ray McDermott, Inc.	\$1,000,000	18 U.S.C. 1952 18 U.S.C. 1343 18 U.S.C. 610 31 U.S.C. 1101 31 U.S.C. 1058
6/23/81 date of judgment	DOJ, Fraud Section	General Electric Company	\$ 31,000**	18 U.S.C. 371, 1341, 1343, 1952
6/23/81 date of judgment	DOJ, Fraud Section	Hoyt P. Steele	\$ 31,000** 4 mos. imprisonment	18 U.S.C. 371, 1341, 1343, 1952

* Penalties include criminal fines, civil penalties, and civil settlements.
 ** Defendant found guilty after trial.

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<u>DATE</u>	<u>PROSECUTION</u>	<u>DEFENDANT</u>	<u>PENALTIES</u>	<u>CHARGE</u>
6/23/81 date of judgment	DOJ, Fraud Section	Robert P. Naples	\$ 31,000** 2 mos. imprisonment	18 U.S.C. 371, 1341, 1343, 1952
6/23/81 date of judgment	DOJ, Fraud Section	Charles Mothon	\$ 31,000** 1 yr. imprisonment	18 U.S.C. 371, 1341, 1343, 1952
6/23/81 date of judgment	DOJ, Fraud Section	Schenectady Turbine Services, Ltd	\$ 31,000**	18 U.S.C. 371, 1341, 1343, 1952
9/8/81 date plea filed	DOJ, Fraud Section	McDonnell Douglas Corp.	\$1,255,000	18 U.S.C. 371, 1001, 1341, 1343 (371 count dismissed)
9/8/81 date of dismissal	DOJ, Fraud Section	James S. McDonnell	Charges dismissed on motion of the government	18 U.S.C. 371, 1341, 1343
9/8/81 date of dismissal	DOJ, Fraud Section	Charles M. Forsyth	Charges dismissed on motion of the government	18 U.S.C. 371, 1341, 1343

* Penalties include criminal fines, civil penalties, and civil settlements.

** Defendant found guilty after trial.

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<u>DATE</u>	<u>PROSECUTION</u>	<u>DEFENDANT</u>	<u>PENALTIES*</u>	<u>CHARGE</u>
9/8/81 date of dismissal	DOJ, Fraud Section	John C. Brizendine	Charges dismissed on motion of the government	18 U.S.C. 371, 1341, 1343
9/8/81 date of dismissal	DOJ, Fraud Section	Sherman Pruitt, Jr.	Charges dismissed on motion of the government	18 U.S.C. 371
10/22/81 date of plea	DOJ, Fraud Section	Sherman Pruitt, Jr.	\$ 40,000 6 months suspended sentence	18 U.S.C. 401

* Penalties include criminal fines, civil penalties, and civil settlements.

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thorized it or, as I suggested earlier in talking to the SEC, sort of the head-in-the-sand approach?

Mr. ROSE. Well, there is no effort here to encourage or condone a head-in-the-sand approach to this problem. What we are trying to do is simply not make the reach of the statute so broad that it prohibits—small businesses, for example, simply cannot afford to have in place an American national to be the sales representative in each and every country where they might want to do business. Under this statute a number of businesses, I think of some size, just simply conclude it is a lot easier, rather than dealing with a criminal statute, to just not be involved in the export trade where there might be a problem of the kind we are talking about.

I am not sure that we should try to reach the outer limits of the kinds of things that you are talking about. If there is winking of a direct nature—we run into this in the antitrust cases all the time, of course, because the higher level officials in a corporation often try to insulate themselves in an antitrust situation, pricefixing or otherwise, from criminal liability. And you simply have to go through the corporation and get witnesses to say what the conduct or understanding of the particular corporate officer who is the target of the investigation is.

We run into that problem of indirect and circumstantial proof in a number of criminal contexts, and I do not think that this language would be any more difficult than trying to enforce the Sherman Act, for example.

Mr. WIRTH. The reason I am asking that is in line with your reacting to language, if and when a Senate bill is passed, the question of agents and where that frontier is.

Mr. ROSE. Is an important one.

Mr. WIRTH. Is an important one, and I raise that because it seems to me that that is the area, according to the cases that you all sent up to us, where most of the activity is. How do we define the relationship between a corporation, an agent, and that set of responsibilities? That is just what you are addressing and I understand it is very tough.

But I raise that as a special area that it seems to me we have to look at very carefully.

Mr. ROSE. I agree with you and we shall do that.

Mr. RINALDO. I think that there has been substantial testimony to the effect that exports, at least by small companies, would increase if there were more certainty in the act. But I am also concerned about enforcement and prosecutions.

In your view, would enforcement of the act and prosecution for violations be more effectively carried out if the act were amended to clear up some of the ambiguities that we have heard about today and to eliminate the uncertainties that currently exist and which are so evident in the act?

Mr. ROSE. Well, I am always—as I said earlier, Mr. Rinaldo, I think the core conduct that we are trying to get at here, namely bribery of foreign officials by U.S. nationals in order to benefit their own businesses, the core examples of that are clearly prohibited under the current law.

The difficulty I have as a prosecutor and what makes me uncomfortable about the statute as it is drafted is that when you start

dealing with areas that are not core conduct or core prohibited conduct, it troubles me to have to rely, it would trouble me even as a prosecutor, and it would trouble me even more as a private lawyer to try to advise a client to rely simply on prosecutorial discretion as the reed upon which you advise a client that it is perfectly all right to engage in certain kinds of payments abroad and that they cannot and will not involve you in any violation of the Foreign Corrupt Practices Act.

The way the statute is currently drafted, you are simply relying on the fact that the Justice Department, in the exercise of its wisdom and judgment, which I think we have and do exercise, simply will not bring prosecutions. Now, you cannot as a private lawyer responsibly and ethically advise somebody to rely on prosecutorial discretion in order to authorize certain kinds of business transactions.

And I think you are exactly right, that what happens instead is that a number of companies who simply cannot afford accounting fees, legal fees—and we were talking about the impact of the act earlier and I think it is important to point out that there has been a tremendous effort. From my personal experience, all of our major clients in my last job as a partner in a law firm spent many sums of money, both with our firm and with accountants, to comply with this act and operate in good faith.

People that cannot afford this kind of money to analyze particular transactions and so forth, simply say, look, I am not going to get involved with the kind of situation that could bring me within the reach of the statute, so therefore I will forego the export opportunity. And obviously, cumulatively these things will add up to a severe impact upon exports and the American economy.

My trouble is that I also would point out that I could not in good conscience advise a client to come up here and testify about that, so that you could have empirical evidence that that was going on, because there would be a lot of adverse effects to the company, ranging from publicity to possible liability of a civil or criminal nature, depending on what the example was.

Maybe I can give you just one example and then I will stop. To take an improbable example, if my client was trying to do business in Afghanistan and they were competing there against the Germans and the Japanese and the French, let us say, and the minister of the economy in Afghanistan says, well, I will not clear this transaction unless I get a \$20 payment.

If I ever want to do business in Afghanistan again, because of this law—which I would refuse to make any such payment—I am not going to come up here and tell you that that is a situation that has occurred, because I simply am not going to be in a situation where I am going to forgo all my relationships, commercial and otherwise, over there. I think that is the kind of difficulty that you are into with empirical evidence in this field. It is a very difficult area and I have tremendous sympathy with this subcommittee for trying to tackle it.

It is going to be awfully hard to have parades of examples of the “might have beens except for this law,” I think.

Mr. RINALDO. I have one more question. The act has been criticized for lack of clarity in the area of allowance of courtesy expend-

itures or what is commonly referred to as grease payments. At the time the act was passed the record is clear that such small facilitating payments were intended to be allowed.

Could you describe as a result of your experience the problems with the present language and the uncertainties it has caused? And also, how could the present language be improved?

Mr. ROSE. Well, I think, to take that in two parts, it is clear from the House report last time that facilitating or so-called grease payments of a customary nature to permit or to cause a foreign official to do that duty which he or she ought to perform were not intended to be within the scope of the act. That is clear from the legislative history of the report of this committee.

The problem is that the language of the statute, which when dealing with a criminal statute, again, is the thing one must go to first and really last, the language that is employed to achieve the desired committee result is simply the use of the word "corruptly." "Whoever corruptly offers to pay" is the language that is used, and "corruptly" is then defined in the legislative history as meaning to exclude facilitating or grease payments, because it is meant to interpret the statute as not including those kinds of payments.

Well, as a criminal defense matter in advising a private client, I simply could not tell a client in good conscience that they could make such a payment and then rely on the legislative history to avoid prosecution and possible conviction, or at least investigation, which is really the thing that most companies try to avoid.

Even the expense and ultimate publicity that can result even though grand jury investigations are secret and intended to be so, the problems that can result from that for companies are really very major both in terms of expense and possible exposure to bad publicity. And therefore they would rather have you advise them that there is a possible risk that some prosecutor will think that this is at least worth investigating with a grand jury, and they will say, well, if that is true then I am not going to make this kind of payment and I am simply not going to undertake this kind of business.

That is the difficulty that I have, this rather broad in terrorem effect of a penal statute. Now, if it were not a criminal statute, as I said, I would feel differently about it.

Second, you have asked for suggested improvements. I think that the Chafee-Rinaldo bill is a real effort in this direction to try to define what kind of payments are appropriate and are not subject to the statute. I think the chairman has pointed out that there is room for ambiguity in at least the current Senate version of that bill, at least certain subsections of it.

I think that we can achieve an appropriate legislative result here, and the only message I have been trying to put across this morning is that this is in need of legislative consideration and promptly. I am not trying to impress upon you this morning a specific defined legislative solution. But we would be glad to come back and do that at a future time.

Mr. WIRTH. Do you agree with us that if we are going to do it, let us do it right?

Mr. ROSE. I agree we should do it right. Let us do it soon as well.

Mr. RINALDO. That is a very good note on which to end, and I want to thank you for your very enlightening testimony.

Mr. WIRTH. Thank you, Mr. Rose.

We will stand adjourned until we hear from our good friends downtown.

[Whereupon, at 1:05 p.m., the subcommittee was adjourned, to reconvene upon the call of the Chair.]

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FOREIGN CORRUPT PRACTICES ACT— OVERSIGHT

WEDNESDAY, DECEMBER 16, 1981

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON TELECOMMUNICATIONS,
CONSUMER PROTECTION, AND FINANCE,
COMMITTEE ON ENERGY AND COMMERCE,
Washington, D.C.

The subcommittee met, pursuant to notice, at 9:35 a.m., in room 2123, Rayburn House Office Building, Hon. Timothy E. Wirth (chairman) presiding.

Mr. WIRTH. The subcommittee will come to order, please.

This is our third oversight hearing on the Foreign Corrupt Practices Act.

What we hope to accomplish at this hearing is to determine the impact of the act on American export performance and on our foreign relations.

When the Foreign Corrupt Practices Act was passed by Congress in 1977, it was acknowledged that some business would be lost as a result of the prohibition against overseas bribes. However, at the time, Congress made a determination that national security, foreign policy, and public policy considerations greatly outweighed any potential business losses.

Why, then, are we here today? This administration has suggested that the act has been a major export disincentive and detrimental to American economic interests.

We are told that no one wants to return to bribery—bribery that can weaken political stability and erode popular support of friendly governments, and jeopardize our important foreign policy interests.

We are told, however, that the act is vague and uncertain, and that it is the ambiguities in the act that have caused business to forgo legitimate export opportunities. These are serious concerns, and they deserve the careful review and consideration of the subcommittee. That is why we are here.

As part of our review of these matters, on October 5 we asked for information from the Special Trade Representative and the Departments of Commerce and State, who have taken the lead in supporting amendments to the act. If, as this administration says, the Foreign Corrupt Practices Act is a major export disincentive, certainly they must have information that proves it.

We asked for their response by November 1 and received no responses until December 2.

One thing which I found encouraging was that we learned that total U.S. exports have exploded from \$121.2 billion in 1977 to \$220.7 billion at the end of 1980, an increase of \$100 billion over a 4-year period. U.S. merchandise exports have grown at an average annual rate of 22 percent since 1977, when the act was passed. Some might conclude that, while the Foreign Corrupt Practices Act may not have been the sole contributor to our great increase in exports, at the least it did not hinder exports, which have, as the record shows, gone up dramatically.

We also approached this problem by seeking information about specific instances of business lost as a result of the Foreign Corrupt Practices Act. It was hoped that we could separate out those instances where business was lost, or thought to be lost, because a company in fact failed to pay a bribe—a result intended by Congress—and those instances where business was lost or thought to be lost because of any real or perceived ambiguity in the act.

Unfortunately, the information we were supplied did not answer our questions. We received second- or third-hand anecdotes about business lost, or thought to be lost, as a result of the act. The examples given were selected, edited, and were themselves vague. It is difficult to determine whether losses of business in fact occurred, whether the losses could be attributable to the act, and whether the losses were those intended by Congress or were losses due to uncertainties in the statute.

Still, we will continue to look for facts underlying legitimate complaints. It is incumbent upon us to do so.

Finally, we asked for information from the Department of State on the foreign policy implications of overseas bribery and the impact of the Foreign Corrupt Practices Act. The Department confirmed that bribery of foreign government officials can have important ramifications for our foreign relations, and that the act had reduced the possibility of such occurrences.

What is our charge today? We are committed to take a careful look at the act and its impact. If we all believe, as I think we do, that we must not revisit our original decision to prohibit overseas bribery, then we must sift through the information presented to us. We must narrow the focus of our review to those instances where the act has resulted in business losses which were not intended by Congress. We will continue our review until we are satisfied that we have the facts upon which to act.

One final note: the Senate has already acted in this matter. A number of dedicated and very respected Members of the Senate devoted a great deal of time to working out amendments to the act. Their work deserves a careful review by this subcommittee.

Before proceeding to our first witness, let me ask the ranking minority member, Mr. Collins, if he has any statement he might like to make.

Mr. COLLINS. Thank you, Mr. Chairman. I am glad we could schedule some time this last week of the congressional session in order to have a hearing on this most important Foreign Corrupt Practices Act. I consider a review of this law to be one of the most important matters our subcommittee is undertaking, and I hope that this review will continue and will lead to the consideration of legislation which will revise this statute.

This statute, with the uncertainties it has caused for American companies that do business abroad, has been one of the major export disincentives that is faced by American business. It was identified as inhibiting to export growth by the Carter administration. President Reagan's administration has continued to press for changes to clarify this law. The Senate has recognized the need to amend the law, and last month it passed, by a voice vote, the bill to make a number of improvements in it. Today we are going to hear from some administration witnesses with expertise in the export problems caused by the law as well as the foreign policy implications.

I particularly would like to welcome my good friend Ambassador Bill Brock, who is our U.S. Trade Representative; Sherman Unger, the General Counsel of the Department of Commerce; and Ernest Johnston, the Deputy Assistant Secretary of State for Economic and Business Affairs. We look forward to hearing your testimony.

Again, Mr. Chairman, I would like to emphasize to you my strong interest, which I know is shared by a number of other members of the subcommittee, in moving forward to consider immediately a House bill to amend and improve the Foreign Corrupt Practices Act. I am a cosponsor of such legislation which has been introduced by Mr. Rinaldo of New Jersey, and I hope this bill can be the basis for subcommittee action early in the next session of this Congress.

Mr. WIRTH. Thank you, Mr. Collins. Mr. Bliley.

Mr. BLILEY. No.

Mr. WIRTH. Our first witnesses this morning are our distinguished colleagues, Mr. Bonker and Mr. Mica. Gentlemen, thank you very much for being here bright and shiny on a cloudy morning. It is very familiar to you, Mr. Bonker. Please proceed in any way you wish.

STATEMENT OF HON. DON BONKER, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF WASHINGTON

Mr. BONKER. Thank you, Mr. Chairman. I had wondered whether this morning's session would be delayed or canceled because of the snow. But I recalled that the chairman of the committee is from Colorado, and he is not intimidated by snow.

Mr. WIRTH. I got up early and reveled in the white stuff. The children were delighted.

Mr. BONKER. Mr. Chairman, I have a formal statement I would like to have submitted for the record.

Mr. WIRTH. Without objection, it will be included in full in the record.

Mr. BONKER. I will keep my remarks very brief. I appear this morning as chairman of the House Export Task Force. The task force is concerned primarily with export trade and what this Congress can do to enhance our trade opportunities abroad. We are living in a fiercely competitive world economy. To be more competitive in the world market, the task force has attempted to identify a number of issues which we believe are essential for Congress to address.

We have actually identified six issues, three of which we have placed in a category of disincentives—issues and laws which inhibit our trade potential. One of those issues is the Foreign Corrupt Practices Act of 1977.

Mr. Chairman, I am not familiar with all the details of this act, but I am somewhat acquainted with the environment in the Congress at the time the bill was enacted. We all know that that was a time of widespread revelations in the press about American corporations who were discovered making payments to foreign officials, and particularly in developing countries. One of the best known cases, of course, was the Lockheed scandal in Japan. But the bill was drafted hastily and without the benefit of extensive hearings. Now we have had an opportunity to see this law being implemented, and it is fairly clear that it is ambiguous and confusing.

There are several agencies involved in its implementation. We have problems with the uncertainty regarding cases of bribery. The FCPA is a criminal statute with extraterritorial application, and this must be made clearly discernible when there is a known violation. It is appropriate for Congress to review this law and to modify it so that we can more effectively administer the law and retain its original purpose.

I don't think there is anyone in this body that is going to support bribery in international commerce. It is extremely important that we retain the purposes for which the law was enacted, but by the same token I think that we ought to review the law, to see if there is a way that we can retain its original purpose without encumbering the American business community which is completely at a disadvantage in the world market.

I know there is a provision of the law which instructs our representatives in trade negotiations to involve other countries in adopting similar statutes, so that we could have some consistency. But if our own law is fraught with inconsistency, confusion, and uncertainty, it is going to be extremely difficult to achieve that consensus.

Mr. Chairman, I have seen some reports on the FCPA, and it has been fairly well documented that we have lost or we are losing somewhere between \$1 and \$2 billion a year in business activity, and that doesn't really include business opportunities that are lost because of the intimidation that is associated with this statute.

The statistics also show that for every billion dollars in international trade involving U.S. businesses, it translates into about 26,000 or 27,000 jobs. If we are going to realize our export potential, if we are going to become more competitive on the world market, if we are going to stay abreast of the new industrialized nations, and especially the competitive fervor of the Pacific Rim countries, which is really driving us off the economic map, we have got to encourage business activity in the world market. We are going to have to remove some of the disincentives.

If we are going to realize our full economic potential in our domestic economy, I think we have to enhance our international trade possibilities.

The task force has identified three issues which we consider disincentives. Two of those disincentives Congress has already dealt with in some form. One is the taxation on U.S. nationals who are

working abroad, and the second is the export controls, notably the Export Administration Act. This is another example of a law which plagues the business community by requiring them to apply for export licenses. We have attempted to reform that law, in a realistic and practical way that is making it possible now for more expeditious action when those cases involving export licenses are involved.

This is the third statute identified by the task force which needs to be closely scrutinized by Congress. We support a review and modification of the FCPA in order to provide for an efficient internal reporting and accounting system under the Securities and Exchange Commission, without the criminal provisions of the statute which should be retained with the Justice Department.

In closing, I know your staff has followed the Senate hearings and realizes that the bill has gone through an extensive process and has been amended to make it more acceptable by Members of the other body. I can't recall the vote in the Senate, many Democrats did vote for the final version. On the floor Senator Proxmire had several amendments adopted that I think made it more palatable.

It is important that we even change the name of the statute so it doesn't imply something simply by conforming to its provisions. I am not sure I like the title that has been attached in the Senate. It is lengthy. Maybe I would just say the Foreign Trade Reporting Act. But that is just a matter of semantics.

I think the provisions in the Senate bill are realistic and I think should be acceptable by the House as a whole.

Mr. Chairman, I hope that when you take up this issue—and I hope you do take it up—you will remember that the Export Task Force, which is now representative of over 100 Members of this body covering every part of the political spectrum, would very much like to see some major reform of this law, so that we can get on with the business of encouraging our export potential in the world market.

Thank you.

[Mr. Bonker's prepared statement follows:]

STATEMENT OF
CONGRESSMAN DON BONKER
CHAIRMAN OF THE HOUSE EXPORT TASK FORCE
BEFORE THE HOUSE SUBCOMMITTEE ON
TELECOMMUNICATIONS, CONSUMER PROTECTION, AND FINANCE

DECEMBER 16, 1981

MR. CHAIRMAN, I AM PLEASED TO APPEAR TODAY BEFORE THE TELECOMMUNICATIONS, CONSUMER PROTECTION AND FINANCE SUBCOMMITTEE OF THE HOUSE ENERGY AND COMMERCE COMMITTEE. I APPRECIATE THE OPPORTUNITY TO TESTIFY, AS CHAIRMAN OF THE HOUSE EXPORT TASK FORCE, ON THE NEGATIVE EFFECTS THE FOREIGN CORRUPT PRACTICES ACT (FCPA) OF 1977 HAS HAD ON U.S. BUSINESS AND AMERICA'S ROLE IN INTERNATIONAL TRADE.

MR. CHAIRMAN AND DISTINGUISHED MEMBERS OF THE SUBCOMMITTEE, BEFORE I DISCUSS SPECIFIC PROBLEMS WITH THE FCPA, I WOULD LIKE TO PROVIDE YOU WITH THE BACKGROUND AND CLIMATE UNDER WHICH THE FCPA WAS ENACTED.

IN 1973, WITH WATERGATE ON THE FRONT PAGES IN MANY NEWSPAPERS AND STILL A VIVID MEMORY, OVER 300 AMERICAN CORPORATIONS WERE DISCOVERED MAKING PAYMENTS TO FOREIGN OFFICIALS, PARTICULARLY IN DEVELOPING NATIONS. ONE OF THE BETTER KNOWN CASES WAS THE LOCKHEED AIRCRAFT CORPORATION'S DEALINGS WITH CERTAIN JAPANESE OFFICIALS, PUBLICITY AND INVESTIGATION ABOUT WHICH ULTIMATELY LED TO THE DOWNFALL OF THE TAJUKA GOVERNMENT.

SUBSEQUENT INVESTIGATIONS AND REVELATIONS LED TO AN INCENSED AMERICAN PUBLIC... INCENSED WITH THE CORRUPTABILITY OF CORPORATE EXECUTIVES. WHERE WAS OUR SENSE OF

MORALITY? WAS THERE NO LONGER ETHICAL CONDUCT IN BUSINESS? IN GOVERNMENT?

AN OUTRAGED PUBLIC DEMANDED CHANGE, AND IN RESPONSE, FORMER PRESIDENT FORD APPOINTED A TASK FORCE ON QUESTIONABLE CORPORATE PAYMENTS TO ASSESS THE NEED FOR A NEW U.S. LAW TO ADDRESS BUSINESS PAYMENTS. THE TASK FORCE DECIDED THAT EXISTING U.S. LAWS WERE INEFFECTIVE IN DETERRING QUESTIONABLE PAYMENTS BY AMERICAN BUSINESSMEN AND THAT A LAW WAS IN FACT NEEDED TO RESTORE PUBLIC CONFIDENCE IN THE U.S. GOVERNMENT AND IN U.S. BUSINESS CONDUCT.

CONGRESS, TRYING TO APPEASE THE OUTRAGED PUBLIC, HURRIEDLY DRAFTED LEGISLATION, THE FOREIGN CORRUPT PRACTICES ACT OF 1977. I SAY HURRIEDLY BECAUSE VERY LITTLE CONSIDERATION OR THOUGHT WAS GIVEN TO THE POTENTIAL CONSEQUENCES OF THE ACT, IN TERMS OF ITS MEANING, CLARITY, AND APPLICABILITY. AS A RESULT, WE HAVE TODAY AN ACT WHICH IS ONE OF THE MOST POORLY WRITTEN PIECES OF LEGISLATION. ITS LACK OF SPECIFICITY AND AMBIGUOUS WORDING HAVE MADE IT A MAJOR IRRITANT AND COST FOR U.S. BUSINESSES. MOREOVER, IT IS A DISINCENTIVE TO AMERICAN EXPORT TRADE.

SINCE ITS ENACTMENT, THE ACT'S PROVISIONS HAVE BEEN STEEPED IN CONTROVERSY AND CONFUSION OVER WHAT CONSTITUTES COMPLIANCE.

MR. CHAIRMAN, A NUMBER OF REPORTS HAVE BEEN WRITTEN ON THE EFFECTS OF THE FCPA ON AMERICAN BUSINESS OVERSEAS. THE STATE DEPARTMENT CONDUCTED A SURVEY IN MAY OF 1981 IN WHICH 115 FOREIGN SERVICE POSTS ABROAD WERE ASKED TO ASSESS THE EFFECTS OF THE FCPA ON U.S. EXPORTS AND FOREIGN RELATIONS. BY COMPLYING WITH THE ACT, ACCORDING TO THE REPORT, AMERICAN FIRMS FACE A NUMBER OF PROBLEMS, INCLUDING THOSE RELATED TO OBTAINING AND DEALING WITH AGENTS, CONTRACTING PROBLEMS, INCREASED OPERATING COSTS

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FOR ACCOUNTING AND REPORTING REQUIREMENTS, THE LACK OF FLEXIBILITY TO PROVIDE LEGITIMATE GIFTS, AND OVERCAUTIOUSNESS IN ATTEMPTING TO COMPLY WITH THE ACT. THE LATTER SEEMS TO CONFIRM THE FREQUENTLY HEARD COMPLAINTS BY BUSINESS THAT THE ACT IS AMBIGUOUS AND DIFFICULT TO UNDERSTAND.

THE RESULT OF THESE DIFFICULTIES? U.S. FIRMS HAVE:

- FOREGONE SOME APPARENTLY LEGITIMATE EXPORTS,
- AVOIDED SOME MARKETS, AND
- OPTED TO PLAY SUBORDINATE CONTRACTING ROLES TO FOREIGN PRIME CONTRACTORS.

THE FCPA HAS A MORE WIDE-RANGING NEGATIVE EFFECT IN TERMS OF AN AMERICAN FIRM'S LEGITIMATE GROWTH THROUGH ACQUISITION OF A FOREIGN FIRM. LET ME GIVE YOU A RECENT EXAMPLE.

AN AMERICAN FIRM WAS PROHIBITED FROM BUYING OUT A BRITISH FIRM^{in part} BECAUSE OF THE LATTER'S POTENTIAL LOSS OF BUSINESS RESULTING FROM ITS COMPLIANCE WITH THE FCPA-- AN AMERICAN LAW. IF I MAY BE PERMITTED, MR. CHAIRMAN, I WOULD LIKE TO READ FROM THE REPORT ON THE PROPOSED MERGER OF ENSEARCH CORPORATION AND THE DAVY CORPORATION LIMITED, SUBMITTED BY THE BRITISH MONOPOLIES AND MERGERS COMMISSION.

DAVY BELIEVED THAT THE FOREIGN CORRUPT PRACTICES ACT WAS SO FORMULATED THAT IT WOULD ALSO HAVE AN ADVERSE EFFECT ON DAVY'S LEGITIMATE TRANSACTIONS IN A NUMBER OF IMPORTANT OVERSEAS MARKETS, EVEN WHEN THERE WAS NO NEXUS WITH UNITED STATES COMMERCE, IN VIEW OF THE LIABILITIES ON THE OFFICERS AND EMPLOYEES OF UNITED STATES PARENT COMPANIES FOR THE

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ACTS OF FOREIGN SUBSIDIARIES OR BUSINESS PARTNERS WHEN THEY KNOW OR "HAVE REASON TO KNOW" OF THE LATTER'S ACTIVITIES AND OF THE NEED TO ENSURE THAT DETAILED RECORD-KEEPING AND CONTROL SYSTEMS WERE ADOPTED. DAVY HAD BEEN ADVISED THAT THE LANGUAGE OF THE ACT WAS VERY GENERAL AND COMPREHENSIVE WHILE THE POTENTIAL PENALTIES, EVEN FOR TECHNICAL AND INSIGNIFICANT ERRORS, WERE SEVERE. DAVY POINTED OUT THAT MUCH CONFUSION AND UNCERTAINTY SURROUNDED THIS WHOLE AREA OF THE LAW (INCLUDING SUCH ISSUES AS WHAT CONSTITUTES A "CORRUPT" PAYMENT, PARTICULARLY IN COUNTRIES WHERE GIFTS WERE NORMAL AND PERMISSIBLE UNDER LOCAL LAW, OR WHAT CONSTITUTES A "FOREIGN OFFICIAL", PARTICULARLY WHERE THE LINE BETWEEN PERMITTED PUBLIC AND PRIVATE ACTIVITIES WAS UNCLEAR AND WHERE INDIVIDUALS WERE FREE TO ENGAGE IN PUBLIC AND PRIVATE ACTIVITIES AT THE SAME TIME). DAVY MADE EXTENSIVE USE OF AGENTS IN UNDERDEVELOPED OR DEVELOPING COUNTRIES BUT THERE WAS LITTLE DOUBT THAT ENSEARCH WOULD BE BOUND TO INSIST ON THE STRICTEST COMPLIANCE AND, AT THE VERY LEAST, WOULD BE COMPELLED TO EXERCISE CLOSE CONTROL OVER THE WAY IN WHICH DAVY MANAGED ITS OVERSEAS MARKETING OPERATIONS.

MR. CHAIRMAN, THE MONOPOLIES COMMISSION REJECTED ENSEARCH CORPORATION'S BID FOR ACQUISITION OF DAVY IN AUGUST OF THIS YEAR, HINTING THAT THE U.S. FOREIGN CORRUPT PRACTICES ACT LEAVES U.S.-OWNED COMPANIES WITH ONE HAND TIED BEHIND THEIR BACKS WHEN TRYING TO WIN ORDERS.

I HAVE TESTIFIED THAT THE FCPA IS AMBIGUOUS AND UNCLEAR, AND I WOULD LIKE TO TELL YOU WHY. THE ANTIBRIBERY PROVISIONS FORBID PAYMENTS TO AGENTS OR INTERMEDIARIES

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OR TO ANY PERSON WHEN THE PAYING COMPANY OR INDIVIDUAL "KNOWS OR HAS REASON TO KNOW" THAT ALL OR PART OF SUCH PAYMENT WILL BE OFFERED TO A FOREIGN OFFICIAL OR PARTY TO INFLUENCE HIS DECISIONS OR USE HIS INFLUENCE OVER OTHERS.

THE "REASON TO KNOW" STANDARD HOLDS U.S. FIRMS RESPONSIBLE FOR THE ACTIONS OF ANY INTERMEDIARY OR AGENT IT USES TO FACILITATE OVERSEAS BUSINESS. REGARDLESS OF THE STEPS TAKEN BY THE COMPANY TO CONFIRM THE TRUSTWORTHINESS OF AN AGENT, WHEN THE AGENT COMMITS AN IMPROPRIETY THE U.S. CORPORATION IS, UNFAIRLY, HELD ANSWERABLE UNDER THE FCPA. MOREOVER, THE ANTIBRIBERY PROVISIONS ARE UNCLEAR IN TERMS OF WHAT CONSTITUTES A BRIBE AND WHAT IS ACCEPTABLE AS A GREASE PAYMENT OR GIFT. IN MOST DEVELOPING COUNTRIES, GREASE PAYMENTS ARE PERFECTLY ACCEPTABLE AND OFTEN USED TO EXPEDITE THE WORK OF LOWER OFFICIALS, AND GIFTS ARE A PERFECTLY LEGITIMATE BUSINESS COURTESY.

ANOTHER MAJOR PROBLEM LIES WITHIN THE ACCOUNTING PROVISIONS WHICH APPLY ONLY TO COMPANIES REGISTERED WITH THE SEC. THESE COMPANIES MUST KEEP DETAILED BOOKS AND ACCOUNTS WHICH ACCURATELY REFLECT ALL TRANSACTIONS AND THE DISPOSITION OF ASSETS. FIRMS ARE REQUIRED TO DEVISE AND MAINTAIN A SYSTEM OF INTERNAL ACCOUNTING CONTROLS SUFFICIENT TO PROVIDE "REASONABLE ASSURANCES" THAT TRANSACTIONS ARE EXECUTED IN ACCORDANCE WITH MANAGEMENT'S GENERAL OR SPECIFIC AUTHORIZATION.

MR. CHAIRMAN, THE "REASONABLE ASSURANCE" TEST IS VAGUE AND IS TOO DISPOSED TO SUBJECTIVE INTERPRETATION. BUSINESS MANAGERS CANNOT TELL WHAT IS REASONABLE IN THE EYES OF THE SEC. CONSEQUENTLY, THEY TEND TO ERR ON THE SIDE OF "EXCESS" WHEN INTERPRETING REASONABLENESS. THE COST OF AN INTERNAL ACCOUNTING CONTROL SYSTEM UNDER THIS TEST IS IN SOME CASES EXORBITANT, RUNNING INTO THOUSANDS OF DOLLARS.

MR. CHAIRMAN, THE FOREIGN CORRUPT PRACTICES ACT OF 1977 IS CONSIDERED A MAJOR DISINCENTIVE TO EXPORTS BECAUSE OF UNCERTAINTY WITHIN THE BUSINESS COMMUNITY ABOUT THE MEANING AND APPLICATION OF SOME OF ITS KEY PROVISIONS. CONDUCT PROHIBITED AND CONDUCT PERMITTED IS UNCLEAR. THE PROBLEM OF UNCERTAINTY IS COMPOUNDED BY A LACK OF GUIDANCE FROM THE ENFORCEMENT AGENCIES AS TO PROPER INTERPRETATION OF THE ACT'S PROVISIONS. THIS PROBLEM, IN TURN, IS EXACERBATED BY THE DUAL ENFORCEMENT AUTHORITY OF THE JUSTICE DEPARTMENT AND THE SECURITIES AND EXCHANGE COMMISSION OVER THE ACT'S PAYMENTS PROVISIONS.

MR. CHAIRMAN, WE MUST TAKE STEPS TO REMOVE THOSE DISINCENTIVES TO EXPORTS CAUSED BY THE FOREIGN CORRUPT PRACTICES ACT OF 1977. THE AMERICAN BUSINESSMAN HAS THE RIGHT TO KNOW SPECIFICALLY WHAT THEY CAN AND CANNOT DO IN INTERNATIONAL BUSINESS.

THANK YOU, MR. CHAIRMAN, FOR THE OPPORTUNITY TO TESTIFY BEFORE YOU AND YOUR SUBCOMMITTEE ON THIS IMPORTANT ISSUE.

Mr. WIRTH. Thank you very much, Mr. Bonker. I think that this subcommittee clearly shares with the Export Task Force concern about U.S. trade around the world, and increasing the incentives and decreasing the disincentives or inhibitions to trade. The question that we face is the reality of the inhibition of the Foreign Corrupt Practices Act, or whatever we might call the law.

Discussions regarding changing the title itself, might be likened to calling tax increases "revenue enhancement." I think Senator Proxmire clearly said if we are concerned with foreign corrupt practices, let's call it that and be very clear about it. The semantics, I think, as you point out, aren't nearly as important as the substance.

What we are concerned about is how to document the inhibitions or the disincentives to trade. We would like to get from you or from the staff of the Export Task Force, the source of the \$1 to \$2 billion figure of lost exports to which you referred. We have had difficulty getting that figure pinned down, as well as what exactly the figure represented.

We would also like to, if we might, get from you a sense of what are the inhibitions to U.S. exports. You were talking, I think, just about the legislative pieces. Aren't there other inhibitions as well that may rank as deserving of great attention; for example, the research and development that we are doing in this country? Here we are at a time when we are dramatically cutting our national commitment to research and development by gutting the National Science Foundation and by slowing down or stopping all of our investments in NASA. At a time when the administration is talking about disincentives, one of the major things it is doing is cutting off a whole area that serves as a base for our export development; namely our whole university retooling programs, and the graduate student training program.

It seems to me these cuts are very clear disincentives, along with the inflation rate in this country, the deficit, and the value of the dollar. These are, obviously, very major issues that have to be looked at when examining incentives or disincentives, and all these disincentives must be ranked in relationship to the other items that you discussed.

Mr. BONKER. Mr. Chairman, you are preaching to the choir.

Mr. WIRTH. I know.

Mr. BONKER. I would place the research and development, which I think is incredibly important if we are going to realize our trade potential in the category of the productivity, an issue also before the task force. I wouldn't necessarily identify it as a disincentive.

It should be an incentive, an example of what the government could do to enhance our trade opportunities. Anyone can look briefly at the Japanese experience and other modern industrialized countries, and see that research and development is based upon high educational standards.

With respect to the \$2 billion figure, that comes from the Emergency Committee for American Trade. Last spring, that organization surveyed its members, and in response a number of companies estimated that the ambiguities of FCPA were a factor in the loss of business, and that totaled up to \$2 billion. I know that is not terri-

bly scientific, but our task force has worked with the Emergency Committee and we find them to be highly reliable.

Mr. WIRTH. I am not questioning the reliability of that. There have been a lot of discussions regarding what do you think about this and what do you think about that. We talk about documenting this and pinpointing it to \$1 or \$2 billion and so many jobs. It seems to me we have to be very careful and separate out what is opinion from what we know to be fact, and that is extremely difficult.

We have had a very difficult time doing that. We have had numerous talks with the Special Trade Representative and the Department of Commerce in attempting to pin down what is real and what is not real in all of this. That is a chore that we face and that, it seems to me, is necessary in order to conduct the careful oversight over this act, as you suggest ought to be done.

Going back to issues such as another area clearly is marketing. One of the things in an increasingly competitive environment is that we have to have more and more people around the world who understand foreign markets and foreign language. Just at the time when that is an increasing necessity in the country we are faced with an administration that is sharply cutting back on foreign language and foreign area training. It doesn't seem to me that this is consistent with the goal of augmenting and increasing our ability to compete around the world.

Mr. BONKER. Mr. Chairman, you are absolutely correct, and I am on the Task Force on International Languages. Again, you are preaching to the choir. Identifying these other issues does not remove our responsibility on one of the major disincentives.

Just like the Export Administration Act, and it is the conservatives in Congress who really want to see that tightened up, is a burden on the business community. We have to identify each of these issues and see what we can do to retain the original intent and the purpose of the act, but without an administrative burden, the duplication of various agencies involved in the accounting requirements and enforcement procedures that we have in this particular case.

I am not saying that we should do away with the act, and I am not saying these other things aren't important. They are important, but we have before your committee a very important act that needs some review and modification, and we need to look at ways in which we can remove some administrative burdens.

The purpose isn't to harass the business community. The purpose is to minimize and, hopefully, eliminate bribery and corruption in international trade.

Mr. COLLINS. Mr. Chairman.

Mr. WIRTH. Mr. Collins.

Mr. COLLINS. I very much appreciate the fact that you bring in an impartial, completely open and a thorough study on this and recommend that we accept the general views, as I understand it, of the Senate. Is that your consensus, that we ought to follow generally, Mr. Bonker, what they did?

Mr. BONKER. My personal view is that the Senate bill is the result of the rather extensive process of hearings and amendments

on the floor, and I think it is acceptable. We have come a long distance from the earlier bill that was introduced in the Senate.

Mr. COLLINS. As it came out of the Senate?

Mr. BONKER. As it came out of the Senate.

Mr. COLLINS. You brought out one thing which I know is very important. You discussed how this bill evolved. It was during the period when we had our troubled times up here in Washington, and as a result of that we reacted. We had problems with people in the Government itself and we had problems with business.

Now this is a very forgiving Congress. Just last week we passed a continuing resolution that gives Members the equivalent of \$10,500 in salary increases and by the same token we should also be forgiving, I think, of business and try to find a way to help them also move down the road.

I agree with one of the thoughts you had, that if we change the name of this bill, it would pass immediately. No one wants to vote for a bill that has anything to do with corruption. But I like your idea about the semantics. I think that is very, very important.

I want to add one other thing. My colleague mentioned the fact that we have been cutting a little on Government spending. We have a deficit, as you know, of \$100 billion right now. We have to cut Government spending, and the only way we can offset it is to increase the activities of private enterprise. This bill would be tremendously helpful. I judge that you have a keen interest in increasing exports. Is that your primary interest in this bill?

Mr. BONKER. That is our sole interest.

Mr. COLLINS. So if we are interested in increasing exports and increasing the activities of private business, this would be a tremendous step forward. I very much appreciate your joining us this morning.

Mr. BONKER. Thank you.

Mr. WIRTH. Mr. Swift.

Mr. SWIFT. Just very briefly, Mr. Chairman.

I want to commend my colleague from Washington State for the leadership that he has taken as chairman of the House Export Task Force. I know the quality of work he is doing, and his views with regard to this legislation will have considerable weight with me and I thank you very much for it.

Mr. RINALDO. Mr. Chairman, I want to thank Congressman Bonker. The testimony that I heard was excellent. He brought the proper perspective before this committee. Over again over again we have heard that the Foreign Corrupt Practices Act in its present form has a number of provisions which are vague and ambiguous, provisions which have led to great uncertainty among American companies who are seeking to comply with the act. I recognize the chairman's difficulty with anecdotal evidence, but I also feel that if the record is examined very carefully, it indicates that there was a lot of anecdotal evidence that went into the debate when the bill was originally passed, and I think possibly a lot of emotionalism. This contributed to the manner in which the bill was passed and the uncertainty that we have in the bill.

As you recognize, the Senate made a number of changes in the legislation as it was originally introduced. Personally, I fully sup-

port those changes. They greatly improve the workability of the statute.

While I fully support those changes, and feel that certain improvements in the act are needed, I would not object to the consideration of additional improvements or any other changes by our subcommittee. Mr. Chairman, I would welcome the opportunity to work with you and all of the members of this subcommittee to make further changes, and to begin consideration of a bill on the House side, so that we can take up what I consider a very needed and urgent modification in the present law.

I want to once again thank you for your very excellent testimony and the perspective that you have brought before this committee.

Mr. BONKER. Thank you.

Mr. WIRTH. Thank you very much.

Mr. BONKER. Mr. Chairman, could I make a very brief parting statement? There is a perception that the people who are victims of this act are the multinational corporations. I think it should be pointed out that the small businesses who are attempting to compete have to comply as well but they don't have all of the accounting and legal resources to do it, and still compete effectively. So I think we have to recognize that the law applies equally to small businesses as well. We are about to pass the Export Trading Company Act in the Congress, which will make it possible for the first time for small- and medium-size companies to compete right alongside with multinationals.

I was talking to our colleague Rick Nolan the other day, who has set up an export trading company in his State. He has a real opportunity to extend the world market to small- and medium-size businesses in this country. But, if we are going to place this administrative burden upon him, including the uncertainties and paperwork that accompany this act, then we are making it more difficult for the small guy to get a piece of the world action, economically speaking. I hope you keep that in mind when you take up the revision of the bill.

Mr. WIRTH. Fine. Thank you very much, Mr. Bonker. We greatly appreciate your being here. As Mr. Swift said, we appreciate your good work with the Export Task Force. Thank you very much.

Mr. BONKER. Thank you.

Mr. WIRTH. Mr. Mica.

STATEMENT OF HON. DAN MICA, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF FLORIDA

Mr. MICA. Thank you, Mr. Chairman. I might say I am not superstitious, but I would like unanimous consent to have the green light during my testimony, if I may.

The chairman knows that I come here as a member of the Foreign Affairs Committee and I tried mightily twice to be a member of the chairman's committee and I probably will try a third time, I don't know yet.

Mr. WIRTH. We look forward to having the gentleman as a member of this very distinguished and omniscient committee under the chairmanship of Mr. Dingell.

Mr. MICA. Maybe I could be an honorary member.

I would like to start out by saying first, particularly because of the chairman's comments when I said I was going to come and testify to this committee, I am against foreign corrupt practices, and I am against domestic corrupt practices, and I am against congressional corrupt practices and individual corrupt practices.

I think it has nothing to do with whether you are for or against corrupt practices. I really think that my colleague, Mr. Bonker and the honorable chairman hit on the subject, the point and the key of this legislation, and that is the attitude that is involved in dealing with this legislation and its ambiguity.

Two Florida Governors have testified that this law needed to be changed. Two administrations have testified that this law needs to be changed. It is not a partisan issue at all, and I might say that when I tried to come on this committee some 2 or 3 years ago now, and again a year ago, I was called on by representatives of the business community and they pointed out some of the concerns that they have with the domestic economy in the United States, and they said, "Stay on the Foreign Affairs Committee."

And I couldn't quite understand that. And their feeling in the business community—and I am talking about small and large—is that for the 1980's the future of this Nation is expanding its trade in world markets.

I was amazed to find out from the U.S. Chamber of Commerce, 1981 was the first year in the history of the U.S. Chamber that more money is going into foreign studies, international trade, than domestic. They think that if America does not turn to the international market, we cannot grow at the levels that we need to grow. So I think that we don't even need to talk about foreign corrupt practices. My druthers would be to change the title totally.

The Wirth committee, with its creativity, with its leadership for the 1980's, could talk about Foreign Trade Incentives and Accounting Act, to try to lead the way, and that is where my background on the Foreign Affairs Committee has given me some insight. I have had some previous travels in Japan, Asia, the Middle East, Egypt, Israel, Saudi Arabia, and unless all of these people have gotten together and decided to tell Dan Mica wherever he stops and gets off a plane that they are afraid of the Corrupt Practices Act, that they don't know what it means, does the committee want them personally to go to jail, then I think the feeling is unanimous outside of this country that there is a problem with this legislation, that we really do need some creativity to make some changes.

Just last week I was in Saudi Arabia—and I thought this was interesting—first, to note the lobby was teeming with businessmen from Germany, from France, from Italy, from Japan, all over the world. All of them are seeking contracts from the Saudi Government. We were invited in to speak to a group of American businessmen in Saudi Arabia. I thought I would walk into a small room with a dozen people for coffee. There were over 500 businessmen in that room. For every single one of them the only topic that they wanted to talk about was the Foreign Corrupt Practices Act.

I started asking where they are from. Were they all Exxon, were they all Mobil? No, they were every kind of company that you could imagine in the United States, some from Florida, one from

my own district, Harris Computer Co., telling us that they have lost untold amounts of business.

Now I don't have the statistics of how much business, and I know that is a concern of the chairman and it is a legitimate concern, but I would like to say at this point I don't know how many opponents I have scared away by my good work in Congress. I don't know how many extra votes the chairman has received because of his masterful work as the chairman. Sometimes statistics don't answer the question, and the question that is posed right now is not a statistical question but, rather, do American businessmen all over the world perceive this to be a law that they can't handle, that they can't deal with, even though they are trying to do a good job.

Now, we could approach it with the idea that all American businessmen overseas are crooks, but I don't believe that and I know the committee doesn't believe that.

We could approach it with the idea that we are going to stop them at every turn in the road. I don't think that that is the will of the American people, the committee, or anyone concerned. My own feeling, after 3 years on Foreign Affairs, visiting these countries, even in Hong Kong, in Japan—and I might add in Japan to hear government officials meeting with every business leader they can meet with, and not say we want to stop, but our policy is to help you get in and crack American markets or foreign markets, and in every law we write we try to have a little committee, a little group, that does something to help the business.

Now, of course, we are talking legally, so I think that we do need to make some changes. I don't come as an expert on this law. I know the outline, I don't know the details, but I have had comments in Florida from my own small companies in Florida. We don't have any real majors there. I have had comments in countries all over the world, and it has become evident to me that the sheer ambiguity of the law has created a major problem. In fact, just this week I asked for several legal opinions on the law, and I was told that lawyers didn't want to venture opinions on the law until they had a specific case, because it is so ambiguous.

Mr. COLLINS. Mr. Chairman, I would just like to have you yield. We have got a vote. Would it be all right, Mr. Mica? We have got 7 minutes.

Mr. MICA. If you will put the green light back on.

Mr. COLLINS. I agree with everything you said. You could talk for an hour the way you are talking.

Mr. MICA. I only have a few more minutes but maybe we had better vote.

[Brief recess.]

Mr. WIRTH. Will you proceed.

Mr. MICA. Thank you, Mr. Chairman.

Just a brief wrap-up, if I may. I might just add with regard to your comments about specific facts, just going over to the House floor I heard an interesting comment. Another one of our colleagues said, "I wonder how many people didn't come to work today because of the snow?"

And another colleague said, "Well, many of them didn't try because they were afraid. They didn't know."

And I think that applies to what we have here today. A lot of them could have made it very easily and they wouldn't have had a problem. They didn't even want to try because there was a doubt, a question.

Two last points quickly. We had a bill regarding illegal immigration in the Foreign Affairs Committee on Haiti, very similar in nature to the controversy surrounding this, and I am very pleased the way we worked it out. It was to stop immigration from Haiti to the United States, which is a problem to Florida, and immediately all of the Black Caucus, the liberals in the House said no way.

So we changed the bill to say it would be a bill to help the Haitian Government, and with the knowledge of Duvalier and so on, the conservatives and others said no way, so we went back to the drafting board and we rewrote the bill and the first thing we did was change the name. It was a bill to promote the development of the Haitian people and to reduce the flow of illegal immigration into this country, and we put in stronger penalties for the government there not cooperating with us, real conditions on the Duvalier regime, and rewards for them working with us.

Now, that bill passed the subcommittee, the full committee, the House and the Senate unanimously, and we started out with a bill that both sides pledged to block on the floor of the House.

I just say to you that one of the keys, I think, is to start to change that name, to change the approach. I heard my colleague, and I would respectfully disagree with the Senate version. This committee, I am convinced, can do a better job than the Senate version. If we have to take a version that would be acceptable, but we can really turn this around and make this the Foreign Trade Incentive and Accounting Practices Act, with real teeth and with a real measure of incentive for our business community, because there is no question that leadership in the 1980's demands changes in many of our laws, expansion in our economy, both domestic and international, and this would be a magnificent place to begin.

Mr. WIRTH. Mr. Collins.

Mr. COLLINS. I appreciate very much your suggestion about the name, and I like it, the Foreign Incentives and Accounting—what was the rest of it again?

Mr. MICA. The Foreign Trade Incentive and Accounting Act. I am open to any new title. I just think the point is that that would be a good one. This committee, I am sure, could come up with a number of recommended changes, but again it comes back to attitude. I think, as was said earlier, this bill is probably a bigger fright to the honest businessman because of its ambiguities than if it were more direct.

Mr. COLLINS. Thank you very much.

Mr. WIRTH. Fine. Thank you, Mr. Mica. Mr. Swift.

Mr. SWIFT. No questions.

Mr. WIRTH. We greatly appreciate your being here, Mr. Mica, and we look forward to working with you on this legislation.

Mr. MICA. Thank you, Mr. Chairman.

Mr. WIRTH. Our next witness is a very familiar figure to everybody on the Hill and is currently the U.S. Special Trade Representative, William Brock.

Mr. Brock, thank you very much for being here. Again, we appreciate your patience and attention to this issue, and I am sorry we were not able to get you on earlier.

**STATEMENT OF WILLIAM E. BROCK, U.S. TRADE
REPRESENTATIVE, EXECUTIVE OFFICE OF THE PRESIDENT**

Mr. BROCK. No problem, Mr. Chairman. I appreciate the chance to be with you today. I am not sure I have to say a word. Dan Mica and Don Bonker have done just a superb job, and I don't believe there is a word they said that I didn't agree with. I will, if I may, make just a couple of comments, but I would basically like to submit my testimony for the record so that we can get to whatever questions you have.

Mr. WIRTH. Without objection, that will be included.

Mr. BROCK. I will be followed, I gather, immediately by Sherman Unger, General Counsel of Commerce, and Ernest Johnston, Deputy Assistant Secretary of State for Urban and Business Affairs, who may have elaborate comments and perhaps even more specific responses if you have questions on proposed changes.

Let me first state that we believe, as our other witnesses have stated, that changes in this law are urgent and necessary. I state that as chairman of the Trade Policy Committee, the interagency trade policymaking body created by the Congress, to indicate the administration support of this position is based upon a full interagency consensus. There is no disagreement among any of the several agencies who have studied the problem.

Clarifying ambiguities in the current law and reducing or eliminating excessive recordkeeping will help in our opinion to accomplish the original intent of the law. What we have proposed, then, is correcting or clarifying changes to the FCPA, not a policy change in the intended final consequences.

We have had 4 years of experience with this law, numerous government, private sector, and independent studies under both Democrat and Republican administrations, and we have found, without any exception at all, in both administrations a feeling that the law has inhibited our ability to be competitive overseas, that it is ambiguous, complicated, and difficult to comply with.

It was a commendable undertaking. I think all of us supported the basic thrust and intent of the bill during its consideration in 1976 and 1977. All of us support the principle that illicit payments, whether foreign or domestic, are unethical, undesirable, and irrational. None of us endorse bribery. None of us intend to condone it for any reason.

The problem is one of uncertainty surrounding the application and enforcement of the Foreign Corrupt Practices Act in different countries and cultures. You are dealing with countries that range from 1 billion people to countries with as few as 47,000 people. The level of officials in those countries varies, obviously, substantially. It is almost impossible for business people to know how to apply the law, and the differentiation between so-called "grease" payments and the corruption of a foreign official.

The problem, thus, is one of uncertainty surrounding application and enforcement of the Foreign Corrupt Practices Act. This was a

finding of a GAO study released earlier this year as well as a conclusion reached by President Carter's Export Council, the Commerce Department "Report on Export Disincentives," the National Governors Association, "Joint Economic Report on the East Asia Mission," and numerous trade associations and business institutions. We have provided to you copies of these studies as well as several other reports to support legislative changes.

Many problems arise from confusion over what makes a payment a bribe. The Congress did try to exempt "grease" payments such as gratuities to get low-level bureaucrats to perform their duties of processing forms, approving licenses or unloading a shipment of perishable goods from a boat in dock, but there is a large gray area between that sort of bureaucratic paper shuffling and the potentially destructive corruption of local officials.

There is also the problem of a firm's liability for the actions of foreign agents overseas.

The U.S. business person is left confused as to what sort of circumstances may some day be sufficient evidence to show he had reason to know of possible wrongdoing before the fact.

It should be noted that we have no similar "reason-to-know" standards of responsibility in our domestic bribery laws. If we deem the standards of responsibility inappropriate in our domestic law, it is far more inappropriate when extended internationally to many different cultures and social structures. These questions of uncertainty are so complex as to have earned the FCPA the reputation of being one of our Nation's most serious export disincentives.

When faced with uncertainty and questions of whether or not to make a particular payment, many of which are a social and business custom and legal in many countries, U.S. firms now play it safe and do not even bother to compete. There is evidence that the act has limited the number of countries in which U.S. firms do business.

As Dan Mica said, I haven't been in my travels this year in a single country in which this was not mentioned by both public officials and our American business community as being one of the most difficult barriers to U.S. competitive viability abroad, nor have they failed to mention the additional cost of complying with the accounting and recordkeeping requirements as the GAO study identified.

Here again, the FCPA demands that the business person determine his own reasonable degree of accurate and fair recordkeeping and internal controls, but to violate the statute one need only to err in keeping company books in the detail to which the Securities and Exchange Commission deems necessary. One need not be engaged in corruption or even in foreign sales to violate the so-called Foreign Corrupt Practices Act. So the name is a misnomer.

You have seen the GAO study. A quarter of the respondents in that study stated that accounting cost increases exceeded 35 percent. Over one-half estimated compliance had increased costs 11 to 35 percent, and over 55 percent of the firms polled said they believed their efforts to comply with the act's accounting provisions have cost more than the benefits received. Anyone who is concerned about American productivity, efficiency, and keeping the cost of doing business down cannot ignore these findings.

In essence, we believe there is a need to modernize and reform this particular legislation. The most severe problem that the U.S. companies encounter with FCPA occur in developing countries, where normal business practices vary widely, and there is a direct, a much more direct government involvement in the day-to-day operation of the economy.

Since 1970, the U.S. share of trade with developing countries has dropped from 22 to 17 percent. These are markets U.S. companies are reluctant to enter, because of the ambiguity surrounding the FCPA. These are also the markets the United States can least afford to forfeit to our competitors. We must establish strong trade ties with these countries if we are to retain our competitiveness, because these are the growth markets of the future.

Incidentally, State and Commerce both have extensive studies to support these statements.

While some have pointed to the increased dollar values, as you did yourself, Mr. Chairman, in your opening statement of U.S. exports, such arguments ignore the fact we have been plagued by large trade deficits year after year. In fact, for every year except one during the last decade, our projections indicate that the combined deficit for 1981 and 1982 could exceed \$60 billion. Reducing our deficit is an important part of our economic recovery. Inflation and interest rates will continue to be affected adversely, if we are not able to compete, to sell as much as we buy from other countries.

All of these trade figures point to the same conclusion. Competition for foreign markets is growing faster. The construction industry which the GAO study singled out as the most effective by FCPA provides a graphic example in the Middle Eastern market. In 1976 the U.S. industry ranked first in its share of construction projects in this region. Today it has dropped to 12th, behind countries like Korea, France and at least 90 others.

In this regard, I recommend to the members of this subcommittee the hearings held last month by the Ways and Means Committee on U.S. Trade Policy. It is clear from those proceedings that the U.S. faces a unprecedented economic challenge.

In sum, FCPA reform legislation should seek to solve the problems which have been identified by studies during the past 4 years, to assure businesses conducting legitimate overseas transactions while retaining the strict prohibitions against bribery of foreign government officials. Such measures must clarify key ambiguities in the law, thereby eliminating gray areas where what is and what is not permissible is currently at best extremely difficult to determine.

Most importantly, any successful reform bill should alleviate the major uncertainty that businessmen are faced with under the FCPA liability, based on having reason to know that a foreign agent was planning to engage in a questionable payment, thereby making the act more compatible with domestic bribery law. The administration believes that there are ways in which the current legislation, S. 708 and H.R. 2530, might be improved. As Assistant Attorney Jon Rose told this subcommittee last month, I will be prepared to submit on behalf of the administration a description of

these proposals for the record at a future date when this subcommittee begins its consideration of specific legislation.

Lastly, let me submit that there is an important international aspect to this decision. Our statement as a nation is clear on the issue of illicit payments, and our leadership toward an international effort in this area will be strengthened when we have demonstrated to our trading partners that it is possible to create a reasonable and fair yet comprehensive and stringent prohibition against the bribing of foreign government officials.

That is not the case today. What we have taught our foreign trading partners is that by writing a bill that is complicated and impossible to enforce and comply with, that they should not support international actions against bribery. As a consequence, we have been utterly unsuccessful in negotiating international agreement to reduce the practice of bribery, and I think our own law has made it more difficult.

Let me conclude my remarks with a reference to my capacity before this committee. Congress made the job of U.S. Trade Representative a permanent Cabinet-level position with direct responsibility to the President because of the importance of promoting and fostering international trade. It is my duty to encourage greater U.S. involvement in foreign markets, to pursue greater openness in markets throughout the world and to identify barriers to trade, no matter where they exist, and to seek elimination of such impediments.

I have come before you today to report on one very serious trade barrier to our exports. I view this problem as no less important than reporting to Congress on foreign subsidies, nontariff barriers that take the form of local content requirements or hidden taxes or standards used by our competitors to exclude U.S. products from their borders.

Mr. Chairman, clarifying the Foreign Corrupt Practices Act may be the most important trade issue before us, because it represents a self-imposed constraint to exports that comes not from the fact that we have chosen to take a strong stand against international bribery, but because we have done so in a self-defeating manner.

I urge this committee to begin legislative hearings on reform of the FCPA as soon as possible.

Thank you.

[Testimony resumes on p. 253.]

[Mr. Brock's prepared statement follows:]

TESTIMONY OF
WILLIAM E. BROCK
UNITED STATES TRADE REPRESENTATIVE

BEFORE A HEARING OF THE
SUBCOMMITTEE ON TELECOMMUNICATIONS CONSUMER
PROTECTION, AND FINANCE
HOUSE ENERGY AND COMMERCE COMMITTEE

Wednesday, December 16, 1981

Mr. Chairman, thank you for this opportunity to present the Administration's position on the issue of illicit payments by U.S. corporations to foreign officials in general, and on the trade implications of the Foreign Corrupt Practices Act.

I am joined by Mr. Sherman E. Unger, General Counsel of the Commerce Department, who will discuss the Department's active involvement in this issue during the past three years, and by Mr. Ernest B. Johnston, Deputy Assistant Secretary for Economic and Business Affairs at the State Department, who will address the foreign relations implications of the Act, and current efforts toward an international agreement prohibiting illicit payments.

Mr. Chairman, let me begin by stating that the Administration firmly believes that legislative reforms to the FCPA are a necessity and strongly supports the proposed changes to the bribery portion of the Foreign Corrupt Practices Act along the lines of those encompassed in S. 708 as passed by the Senate.

As Chairman of the Trade Policy Committee, the interagency trade policymaking body created by Congress, I want to emphasize that our support for this position is based on interagency consensus. The Departments of Justice,

State, Treasury, Commerce and other agencies have studied this issue carefully through the Trade Policy Committee process during two Administrations and are unanimous in their support for reform legislation.

We believe that the actions taken by the Senate on this issue are faithful to the objectives sought by Congress in 1977 in attempting to prohibit illicit payments overseas. We feel that clarifying ambiguities in the current law by limiting excessive recordkeeping requirements which presently go far beyond international transactions, will help to accomplish the original intent of the law. Because there has been so much confusion about the Foreign Corrupt Practices Act, not only has Congress' goal of prohibiting overseas bribes been misunderstood by some but another important goal of the Congress -- namely, export promotion -- has been undermined.

To be sure, the Foreign Corrupt Practices Act, when proposed by this Committee in 1976 and 1977, as a statutory solution to the problem of overseas bribery, was a commendable undertaking.

The FCPA, to no one's surprise, was passed unanimously by Congress in December 1977 following widespread reports of questionable payments in connection with U.S. business activities both at home and abroad. Corporate bribes to foreign officials were perceived by both the Executive and Legislative Branches of Government as unethical, unnecessary to the conduct of business, and harmful to our relations with foreign governments. The FCPA was intended to make certain payments, offers of payments, and

gifts to foreign officials, political parties or political candidates illegal. It also established recordkeeping requirements for all publicly held corporations, regardless of whether a corporation is engaged in international business.

Behind the FCPA's prohibition of bribery were the important objectives of enhancing U.S. national security, foreign policy and economic interests. It was believed that: (a) political controversy due to corruption involving American bribes would endanger the stability of friendly foreign governments or complicate U.S. international relations; (b) successor foreign governments would expropriate the assets of or cancel contracts with U.S. businesses believed to have used corrupt practices, and (c) U.S. economic resources would be misallocated because bribery distorts comparative advantage.

This Administration shares these objectives, and commends the House Commerce Committee for its efforts to deal with a multi-faceted problem four years ago.

I state unequivocally that the Administration supports the principle that illicit payments, whether foreign or domestic, are unethical and undesirable. We do not endorse or condone bribery for any reason.

However, while well-intended, the law has given rise to interpretative and practical problems for firms engaged in overseas business.

Certainly, we are all against bribery and condemn the misuse of an official position for personal or monetary gain.

The problem is one of uncertainty surrounding the application and enforcement of the Foreign Corrupt Practices Act in different countries and cultures. This was the finding of a General Accounting Office study released earlier this year, as well as the conclusion reached by President Carter's Export Council, the Commerce Department Report on Export Disincentives, the National Governor's Association, the Joint Economic Committee report on its East Asian mission, and numerous trade associations and business institutions.

Many problems arise from confusion over what makes a payment a bribe. Grease payments, such as gratuities to get low-level bureaucrats to perform their duties of processing forms, approving licenses, or unloading a shipment of perishable goods from a boat in dock, are specifically permitted on the grounds that petty corruption is often unavoidable. This Committee acknowledged that fact when it wrote the FCPA in 1977.

But, there is a large gray area between that sort of bureaucratic paper shuffling and the potentially destructive corruption of local officials.

There is also the problem of a firm's liability for the actions of foreign agents overseas. It is particularly difficult for a U.S. company, large or small, to protect itself against the behavior of an agent in a foreign nation. Large

corporations use hundreds of sales agents throughout the world. Small companies, often attempting to export for the first time, must rely upon individuals about whom limited information, at best, is available. In both cases, the U.S. businessperson is left confused as to what sort of circumstances may someday be sufficient evidence to show he had reason to know of possible wrongdoing before the fact. This is an unreasonable burden on U.S. firms which makes certainty of compliance nearly impossible.

It should be noted that we have no similar "reason to know" standard of responsibility in our domestic bribery laws. If we deem this standard of responsibility inappropriate in our domestic law, it is far more inappropriate when extended internationally, to many different cultural and social structures.

These questions of uncertainty are so complex as to have earned the FCPA the reputation of being one of our nation's most serious export disincentives. Treatment under the FCPA of a wide variety of gifts and payments such as political contributions, courtesy gifts, tokens of esteem and travel and lodging provided to foreign officials in connection with attendance at business presentations have all been sources of uncertainty. This creates a chilling effect for U.S. firms attempting to sell overseas.

When faced with uncertainty and questions of whether or not to make a particular payment, many of which are a social and business custom and legal in many countries, U.S. firms

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now play it safe and do not even bother to compete. There is evidence that the Act has limited the number of countries in which U.S. firms do business.

In addition, the cost of complying with the accounting and recordkeeping requirements of the Act has placed an excessive burden on all publicly held companies regardless of whether or not they make any foreign sales.

Here again, the FCPA demands that the businessperson determine his own reasonable degree of "accurate and fair" recordkeeping and internal controls.

But to violate the statute, one need only to err in keeping company books in the detail to which the Securities and Exchange Commission deems necessary. One need not be engaged in corruption or foreign sales to violate the so-called Foreign Corrupt Practices Act.

Most alarming is the fact that there has been considerable disagreement among the American Bar Association (ABA), the American Institute of Certified Public Accountants (AICPA) and the Securities and Exchange Commission (SEC) as to a firm's responsibility under the accounting provisions of the law.

The General Accounting Office investigated the impact of the FCPA on American business and published the results in March 1981. The report, which covers almost 200 "Fortune 1000" companies, documents the increased costs incurred by businesses (and in the long run consumers) to comply with the Act's vague standards of accountability. The GAO found:

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- o virtually a quarter of the respondents stated that accounting cost increases exceeded 35 percent;
- o over one-half estimated that compliance had increased costs 11 to 35 percent;
- o over 55 percent of the firms polled said they believe their efforts to comply with the Act's accounting provisions have cost more than the benefits received.

An article in the N.Y. Times business section from last fall adds further evidence to GAO's study. William S. Kanaga, Chairman of the American Institute of Certified Public Accountants, commented on the cost of complying with the FCPA:

If you really want a clean bill of health, you're talking about a lot of money. It can add as much as 50 percent to the audit fee in some cases. So for a major international corporation, the additional cost can be in the millions of dollars.

In reference to the ambiguities embedded in the accounting provisions, Kanaga added:

The Act says its management's responsibility to control the corporate assets. But there's a great deal of fuzziness as to what is adequate control This huge grey area in the present law is why so many corporate boards, to be safe, ordered their auditors to comb through their internal controls from top to bottom.

Costly accounting procedures and ambiguities about what is a bribe not only cause U.S. companies to lose foreign orders, but retard competing in the first place. The problems created by the Act are especially onerous on smaller publicly held companies, and new exporters, who are unable to obtain specialized counsel familiar with the Act's intricacies.

Evidence, both at home and abroad, indicates that we need to make the Foreign Corrupt Practices Act a more sensible law

which reflects a wide range of national policy goals -- creating stronger political and economic ties with our trading partners, increasing exports, and curtailing bribery overseas.

We should also realize that many of the problems we currently face are with developing countries, some of which affect our national security. A recent State Department survey found that FCPA related problems are experienced most by American firms operating in developing countries with which the United States has significant trade interests, primarily in the Middle East and Asia.

The most severe problems that U.S. companies encounter with the FCPA occur in developing countries, where normal business practices vary widely and there is more direct government involvement in the day to day operation of the economy. Since 1970, the U.S. share of trade with developing countries has dropped from 22 percent to 17 percent. These are the markets U.S. companies are reluctant to enter because of the ambiguity surrounding the FCPA. These are also the markets the United States can least afford to forfeit to our competitors. We must establish strong trade ties with these countries if we are to retain our competitiveness because these are the growth markets of the future.

While some critics of FCPA reform point to the increased dollar value of U.S. exports, such arguments ignore the fact that our share of world exports has been declining steadily in recent years.

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For example, in 1960, the United States was the world's largest exporter of manufactures and accounted for 25 percent of the world export market for manufactured goods. By 1970, the U.S. share had dropped to 21 percent. By the mid-1970's, Germany had displaced the United States as the world's leading exporter of manufactured goods and by 1980, the U.S. share had fallen to 18 percent. Some analysts expect Japan to displace the United States in manufactured exports during the 1980's.

During this same 20 year period between 1960 and 1980, both Japan's and Germany's shares of the world's manufactured exports increased. Clearly, the United States has been losing its international competitive position.

The construction industry, which the GAO study singled out as one most affected by the FCPA, provides a graphic example in the Middle East market. In 1976, the U.S. industry ranked first in its share of construction projects in this region. Today it has dropped to twelfth place, behind countries like Korea and France.

U.S. imports continue to exceed exports resulting in large deficits year after year in the merchandise trade balance. Our projections indicate that the combined deficit for 1981 and 1982 could exceed \$60 billion.

All of these trade figures point to the same conclusion: competition for foreign markets is growing fiercer. We must respond to the trade problems that have been identified by government agencies and private sector representatives.

In this regard, I recommend to the members of this Subcommittee the hearings held last month by the Ways and Means Committee on U.S. trade policy. It is clear from these proceedings that the United States faces an unprecedented economic challenge. There is little hope of meeting this challenge if we unnecessarily burden our exporters with costly and ambiguous laws like the FCPA.

FCPA reform legislation should seek to solve the problems which have been identified by studies during the past four years, and to reassure businesses conducting legitimate overseas transactions, while retaining the strict prohibitions against bribery of foreign government officials. Such measures must clarify key ambiguities in the law, thereby eliminating "grey areas" where what is and what is not permissible is currently, at best, extremely difficult to determine.

Most importantly, any successful reform bill should alleviate the major uncertainty that businessmen have faced under the FCPA liability based on having "reason to know" that a foreign agent was planning to engage in a questionable payment, thereby making the Act more compatible with domestic bribery law.

Enforcement of antibribery provisions should be made consistent and predictable by: (1) placing all antibribery enforcement responsibilities under the Department of Justice, (2) authorizing the Department of Justice to issue clear and comprehensive guidelines as to what is permissible conduct and what is not permissible conduct, and (3) providing that the FCPA

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constitutes the exclusive substantive prohibition under the U.S. Code for overseas bribery.

FCFA reform legislation should clarify the status of "grease" or facilitating payments and the scope of the exclusion for such payments. This would help solve the question of "grease" payments, which are legal under current law, but which have been difficult to apply to real life situations.

Amending legislation should also clarify that legitimate business marketing expenses, courtesy gifts, and tokens of regard or esteem do not constitute a violation of the Foreign Corrupt Practices Act. In addition, such legislation should demonstrate common sense and respect for the laws of other nations by excluding the prohibition of payments which are legal in the country where they take place.

The Administration believes that there are ways in which the current legislation, S. 708 and H.R. 2530, might be improved. As Assistant Attorney Jon Rose told this Subcommittee last month, I will be prepared to submit on behalf of the Administration a description of these proposals for the record at a future date when this Subcommittee begins its consideration of specific legislation.

While it is important to delineate the important changes supported or proposed by this Administration, it is perhaps more important to mention what is not changed by reform legislation or by the Administration's recommendations.

Briefly stated, the Foreign Corrupt Practices Act will continue to make it unlawful for any U.S. company or any official, employee, director or shareholder of such company corruptly to pay, give, offer, promise, anything of value to any foreign official for the purpose of influencing any act or decision of that foreign official or inducing the official to violate his legal duty or inducing the official to use his influence with a foreign government in order to obtain, retain, direct or maintain business.

When a U.S. corporation has been found to have violated the law, the penalty is a \$1 million fine. For individuals who commit violations the penalty is \$10,000 and/or 5 years in prison. The United States remains the only country with a strong, pervasive, extraterritorial law specifically designed to outlaw corrupt payments to foreign officials.

Let us remember that there is an important international aspect to this issue. It is in the interest of the United States to pursue an agreement on the problem of illicit payments abroad for two reasons. First, a successful agreement with our trading partners has the potential of eliminating the very real competitive disadvantage that now exists between the U.S. companies and companies of other nations. While this is desirable, we, as a nation, have made a conscious and deliberate decision to prohibit U.S. firms from making questionable payments to foreign officials, no matter what other nations choose to do.

Second, and more important, we should pursue an agreement because the problem of illicit payments used to win sales is an international problem. Bribery, regardless of whether it is made by a U.S. firm or by any other Western country, has national security and foreign relations implications for the United States. The problem of illicit payments is clearly a multilateral one: there is little difference in terms of U.S. national security interests whether a friendly foreign government falls at the hands of a bribe by an American firm or a foreign firm. The FCPA has done little to encourage other nations to subscribe to the U.S. approach toward this problem. In fact, to date, American efforts to achieve an international agreement have not produced results. Developed countries have not followed the example of the U.S. as embodied in the Foreign Corrupt Practices Act. Nonetheless, we maintain that it is an important goal for the U.S. to seek a sensible international solution to this problem.

The State Department is prepared to address the current status of our international efforts. Let us understand that the United States will continue to support and enforce a strong international antibribery law for its own citizens. My office will strongly support the State Department in efforts to work for an international approach.

Our statement as a nation is clear on the issue of illicit payments, and our leadership toward an international effort in

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this area will be strengthened when we have demonstrated to our trading partners that it is possible to create a reasonable and fair, yet comprehensive and stringent prohibition against the bribing of foreign government officials. Once the U.S. business community and the U.S. government stand together in support of a practicable law of this type that respects the laws and customs of other nations, our credibility and influence as a world leader against bribery will be greatly enhanced.

Let me conclude my remarks with a reference to my capacity before this Committee.

Congress made the job of U.S. Trade Representative a permanent Cabinet-level position with direct responsibility to the President because of the importance of promoting and fostering international trade.

In accepting this position, it is my duty to encourage greater U.S. involvement in foreign markets, to pursue greater openness in markets throughout the world, and to identify barriers to trade -- no matter where they exist -- and to seek elimination of such impediments.

I have come before you today to report on one very serious trade barrier to our exports. I view this problem as no less important than reporting to Congress on foreign subsidies, nontariff barriers that take the form of local content laws, or hidden taxes or standards used by our competitors to exclude U.S. products from their borders.

Mr. Chairman, clarifying the Foreign Corrupt Practices Act may be the most important trade issue before us because it represents a self-imposed constraint to exports that comes not from the fact that we have chosen to take a strong stance against international bribery, but because we have done so in a self-defeating manner.

Elimination of the export disincentive aspects of the Foreign Corrupt Practices Act is a priority of this Administration and the Office of the USTR. We urge this committee to begin legislative hearings on statutory reforms to the FCPA as soon as possible.

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Mr. WIRTH. Thank you very much, Mr. Ambassador, and I can assure you that all of the members of this subcommittee share with you the commitment to increasing the position of the U.S. trade around the world, a position which, I think, we all understand has grown very significantly.

I don't think you would disagree with my earlier comment in conversation with Congressman Bonker that since 1977, U.S. merchandise exports have grown at an average annual rate of 22 percent?

Mr. BROCK. I wouldn't disagree with that, except that you haven't discounted for inflation. If you take inflation out the figure is substantially lower than that. I would also point out, as I did in my testimony, that while the absolute dollar value of exports has gone up, our share of the market has gone down. We are losing our competitive position in the world markets, and we have lost it in certain parts of the world, precisely the Middle East.

Mr. WIRTH. Did, in fact, the U.S. share of world markets decline since, for example, the Foreign Corrupt Practices Act was passed? Has it been on the decline?

Mr. BROCK. Yes.

Mr. WIRTH. The Commerce Department figures would suggest that that is not the case, but would suggest that our share of free world exports has increased during the 1977-80 period, and that our primary competitors, the ones that are pointed to on a steady basis, West Germany and Japan, experienced a decrease in their share of the overall world market.

I am talking about absolutes versus percentages. The first figures we referred to were in terms of an absolute increase. We also have data which taxes information into account and also shows an increase for U.S. exports.

The purpose of this, I think is very important. While there may be ambiguities in the legislation, and we have to come back to that, I think it is a little bit disingenuous for anybody to suggest, I am not suggesting you are, that any problems we have around the world in the trade area are the result of the Foreign Corrupt Practices Act.

Mr. BROCK. I completely agree.

Mr. WIRTH. Or to suggest that our role in the world trade economy is declining, where in fact the data would suggest just the opposite.

Mr. BROCK. Mr. Chairman, first, you are right. It would be disingenuous and dishonest to suggest that all of our problems stem from one piece of legislation. They stem from a whole range of factors, but we have already addressed some of those. The Congress addressed one problem earlier this year where it reduced the taxation of Americans working abroad.

In 1979, after we hit those people with what I call double taxation, and not very smart taxation, we lost 40 percent, 39 percent of all the Americans working overseas came home. Now we have already addressed that.

Mr. WIRTH. I understand that.

Mr. BROCK. And I appreciate the support of the Congress in taking that action. It was a very important step. Other things that we have done also make it more difficult for American business.

We export our antitrust laws. We are trying to deal with that with export trading company legislation, but I have yet to find a businessperson of any type in any country that didn't mention this as a barrier to trade and an area of extreme difficulty, if they want to do business, primarily with the developing world.

We are doing pretty well, for example, with Europe, and increasing our trade, in part because the dollar was so weak 2 years ago when the numbers you were citing were particularly valid.

That is less so today, by the way, but it is still true that this bill has its primary application not in the developed countries of the world but in the developing countries of the world that are new to the business practice of trade, new to international code of conduct, and there our share of world markets has declined from 22 percent to 17 percent.

I am not saying this is the whole cause of it. I am saying that we have done less business than we would otherwise have done if we had written a law that businesspeople could understand and comply with.

Mr. WIRTH. I just want to focus on your statement on page 8.

"Our share of world exports has been declining steadily in recent years." Yet, the data submitted to the subcommittee by Commerce and by USTR suggests the opposite, that our share is growing, which has got to be a share not only in terms of Japan, but in terms of those developing markets.

In your testimony you also talked earlier about the deficit of U.S. trade overseas. Now, isn't that overall trade deficit predominantly a function of increased oil imports, and the funds that we are sending out of the country to pay for oil imports?

Mr. BROCK. Yes.

Mr. WIRTH. And that in all of the other areas we are, in fact, doing very well, in services, in manufactured goods and capital goods. These exports are going up very dramatically. The capital goods account has doubled in the last 8 years. The services account is increasing very, very dramatically.

Again, I point out that the deficit is a function predominantly of the oil situation, and I think it is again not appropriate for us to say that the deficit is resulting from the Foreign Corrupt Practices Act, and that there is really a linkage between the two.

The deficit oil situation is one that we have to focus on and we are not doing much about that except for raising prices in this country. We cut all the conservation programs. We have done everything we can other than cutting off that extraordinary dependence. We are spending more money on the military to protect it but not doing much to buffer ourselves against that five and a half barrels of oil a day, almost \$100 billion a year going out.

Mr. BROCK. Let me in part agree and then very specifically disagree. First of all, oil imports have been a major part of our trade deficit. In my own judgment that has been primarily due to the Congress' refusal to decontrol oil and natural gas prices.

That is a different issue, and unrelated to the present matter, but let me correct the record, as I tried to do in my statement.

Twenty years ago, we were the world's largest exporter of manufactured goods. Twenty-five percent of the whole world export market was ours. Ten years later it had dropped to 21 percent. By

the mid-1970's, Germany had taken the lead and passed the United States, and it has a population a third of ours.

Today we have fallen to 18 percent of the trade in world manufactured goods, and Japan will displace us very shortly if the present pattern holds. Our share of world manufactured goods trade has in fact fallen, clearly, specifically, consistently now for a period of time, and let me add that the only reason that your numbers would argue that we are not falling as much as I think we are is because we have been so aggressive in the service area, but I will point out to you that in the services field, we are running into increasingly sophisticated barriers to trade every day.

The Bundestag in Germany just has handed out a regulation saying that U.S. subsidiaries in Germany can't send raw data back to the United States for processing in their computers here. That is going to affect our trade. My point is that you are in a very, very volatile, fast-moving world, and every single impediment that we have put upon ourselves that limits out ability to compete does in fact damage U.S. job creation.

Mr. WIRTH. Mr. Ambassador, I am not disagreeing with you at all about the need for a very aggressive U.S. posture on export trade. The telecommunications legislation which I introduced last Thursday, plays a very major premium on that, as you know, and we are talking about the Foreign Corrupt Practices Act, and the relationship of that to an overall trade issue.

I would suggest that it is very difficult for us to tease out in substantive terms that this act has, in fact, inhibited our exports. In fact, that data is not available, and we have worked and tried to get a handle on it over and over and over again.

We have heard reference over and over and over again to the GAO report regarding the impact of the Foreign Corrupt Practices Act on U.S. business. That GAO report was a survey of business opinion. In asking for loss of business due to the act, the GAO report failed to distinguish between loss due to the prohibition against bribery and loss due to any real or perceived parts of the Act.

Further, in that same GAO report, two-thirds of the respondents said that the Foreign Corrupt Practices Act had little or no effect on business. On the accounting provisions studied in the GAO Act—

Mr. BROCK. Did you notice they were once doing business in Europe, primarily?

Mr. WIRTH. Two-thirds of the individuals said that. Very few respondents said that that was a major inhibition there, and again, the distinction was not made between the antibribery provisions and the ambiguous provisions. The need to separate that out is very clear, I think, and nobody I believe is talking about throwing out the whole piece of legislation.

Mr. BROCK. I accept that.

Mr. WIRTH. Related to the costs of doing business, we had a very thorough discussion here with the Securities and Exchange Commission in which the SEC said that most of the accounting costs talked about in the GAO report are startup costs, which are absorbed, and that the analysis of GAO was not, on its surface, completely fair.

There comments came from the SEC, who is charged with looking at and administering that part of the act.

Mr. BROCK. But you know with all respect to the SEC, they have used the Foreign Corrupt Practices Act as a Trojan horse to get an extension of accounting standards to all companies when they do foreign business at all or not. That is the reason. They have a different attitude on this legislation, but they still say, even the SEC says, that they would like to see a more workable language, as you heard in testimony.

Mr. WIRTH. But again, there is the separation. Let's pin down what is the reality and what is not the reality. We have trouble citing the GAO report as a substantive base for examining the act. Separating out the effects of the bribery provisions and the alleged ambiguities is what we are trying to do. The Carter administration's report of September 1980, which is cited on numerous occasions, was dismissed by the Justice Department.

The Justice Department said:

It was not at all clear that this anecdotal evidence supported the conclusions that were drawn that particular provisions of the act were ambiguous and that ambiguity was causing loss of foreign business unintended by the Congress.

We have, again, a very different problem. What I have attempted to do is, one, gather very specific evidence of problems. This has not been forthcoming. We have not been able to find this evidence either in the chamber's submission or in the submission of the Department of State. We can go through these submissions if you would like.

Second, to put this in the context of overall U.S. trade, we all agree U.S. trade should be increased and be encouraged as much as possible. Is this a very real inhibition? Or perhaps it has had a positive impact on exports? Nobody has looked at the positive side at all. Furthermore, where does this act fall in an overall hierarchy of trade issues? We can come back and discuss these points at length.

I would like particularly, in the little bit of time remaining, to talk to you specifically about language in the legislation, and whether or not you think that this language makes sense in the current Senate bill.

Under section 104(c) of the bill, it says, under the bribery prohibition, "shall not apply to any expenditures including travel and lodging expense associated with the selling our purchasing of goods and services, and with the demonstration or explanation of products."

Is that unambiguous language, do you think?

Mr. BROCK. In the present bill?

Mr. WIRTH. How could we ever convict? This is reading from the bill passed in the Senate, by the way.

Mr. BROCK. I think I would accept what Dan Mica said earlier. I am not at all sure that the language of the bill cannot be improved and made more precise. We would have no reluctance whatsoever to work with you in that regard.

I do think that the Senate bill is less ambiguous, less complicated, and more enforceable than the present law, but if you want to

get down to specifics and work on particular language, we would be delighted to do that with you.

Mr. WIRTH. This language in the Senate bill that a bribe is not an expenditure associated with selling goods and services. There is nothing enforceable about this language whatsoever.

Mr. BROCK. I think you have to take that in the context of the whole bill.

Mr. WIRTH. We had testimony saying there were real problems with—

Mr. RINALDO. Will you yield on that point, Mr. Chairman? I want to say I have read over the section that you just cited. I have to completely agree with you. It is a deficiency in the language in the Senate-passed bill, but I don't think anyone here is contending that we should pass the Senate-passed bill exactly as it is.

If we have hearings this would be one area where we certainly could improve upon the language in the Senate-passed bill, and I would be very willing to work with you on that point when we get to the hearing stage, so that the problems with that language are cleared up, and we have language that is more easily understood.

Mr. WIRTH. I appreciate the gentleman's comments. Let me just respond by saying that when we first got into this 9 months ago, I was told as chairman of the subcommittee that the bill then on the Senate side was the greatest thing since sliced bread, and that we should move it through at extraordinarily high speed. That has changed and we have different language on the Senate side. And now the rat-tat-tat begins that that is the greatest thing that ever came down the line and ought to be passed because it is very specifically enforceable and so on.

You look at the language and it is just as, if not more, ambiguous than what is in the current statute.

Let me give you another example. "Subsections (a) and (b)," which are the antibribery provisions, "shall not apply to any ordinary expenditures including travel and lodging expenses associated with the performance of a contract with a foreign government or agency thereof."

The exceptions we just talked about before can negate the effect of the entire act. We have before us very real ambiguities built into the language on the Senate side, and I am not sure that this bill will really solve anything. We can all feel good about passing a piece of legislation and changing the name of the act, but what we have got is language that creates potentially even greater confusion and uncertainty than we had before.

Mr. BROCK. At least we are making progress, Mr. Chairman. Up until now, I thought you weren't willing to consider legislation. If you are willing to look at it I can get right down to it.

Mr. RINALDO. That presents us with a tremendous challenge to write language that would be an improvement over the Senate bill and clear up some of the problems that you have just mentioned.

Mr. WIRTH. Only if we can propose language that is less ambiguous than language that exists now, that is enforceable, and that the evidence suggests would address whatever problems might exist.

The gentleman from Texas.

Mr. COLLINS. I appreciate very much the comments you have made and I think that would be a good place to start. Change that

one section and then we could just adopt the bill. This bill is so essential, and I am so glad the Ambassador visited with us. I wanted to tell you that the chairman and I disagree on some of the issues that he has brought up. He talked about the Carter administration as a place of reference. I was amazed that the Justice Department had time to study this subject. Every time I talked to them they were working on busing down there.

It was in their dying days that they made this survey. If ever there is a group that didn't know much about business, it was the Justice Department under Carter's administration, and I will tell you what happened to business during that period.

When they left, the prime interest rate was 21 percent. I am glad that you are concerned about how we can get more jobs for America and how we can build business for America.

The one thing that we passed over lightly, and yet it is the whole essence of this, is what has happened because of oil imports. In 1973, we got into a system of increased government regulation. You were in the Senate at that time.

You will remember that we were importing \$3 billion of oil per year. This year we are going to import approximately \$100 billion, aren't we?

Mr. BROCK. We have done better. We have cut it back. It is probably going to be around \$80 billion, I would imagine.

Mr. COLLINS. \$80 billion?

Mr. BROCK. Too much.

Mr. COLLINS. We reached \$100 billion last year, and under President Reagan's administration we are now having conservation. Hasn't open pricing done a lot to bring about conservation?

Mr. BROCK. Yes, sir, absolutely.

Mr. COLLINS. We have seen that turn around, but we still have that \$80 billion. I have heard all these statistics about how we are now shipping more goods. All we are doing is shipping more goods to try to pay for all this oil that is flowing into this country, aren't we?

Mr. BROCK. We are trying to.

Mr. COLLINS. What is the situation, for instance, in the Arab countries, just to take a specific example? How much oil do they ship us and how much do we ship back in the way of goods? Is it an offset or are we running a deficit paying for that oil?

Mr. BROCK. We have an enormous deficit.

Mr. COLLINS. So when you talk about that area, we do not have an equal trade basis?

Mr. BROCK. As a matter of fact, we have gone from being the overwhelming competitor, for example, in construction in the Middle East, as I said, to being the 12th largest competitor in that area, and are down to something well under 5 percent of their total business, whereas before we had a majority of the total basis.

Mr. COLLINS. Here we are the biggest customer, and yet when it comes to paying for it, we are running No. 12. Well, I will tell you, you know what they are doing to get the rest of it. They are taking over all the farms in this country, the lands in this country, the shopping centers, the office buildings.

What we would rather do would be to pay for it with goods and services, and I think the Ambassador has exactly the right approach with this bill.

You mentioned you have seen several specific instances of lost business because of the FCPA. You might just outline for the committee, some of the specific situations which have arisen as a result of this law.

Mr. BROCK. I am a little surprised that we are charged with not having specifics. We have submitted to the committee several examples of lost trade that are specific. I will give you just one example, and I will just pick it at random here.

Mr. RINALDO. Will the gentleman yield?

Mr. BROCK. Yes.

Mr. RINALDO. I believe, Mr. Chairman, he is probably going to refer to the examples of lost trade and increased costs credited by the FCPA which is in attachment 1 of the information submitted to the subcommittee. I want to say, Mr. Ambassador, I have read that. They are excellent examples, and I know you are probably going to discuss a few of them, but I would request at this point unanimous consent that attachment No. 1 be included in its entirety in the record.

Mr. WIRTH. Without objection it will be included.

[The following attachment 1 was received for the record:]

THE UNITED STATES TRADE REPRESENTATIVE
WASHINGTON
20506

ATTACHMENT 1

EXAMPLES OF LOST TRADE AND INCREASED COSTS CREATED BY THE FCPA

-- Disincentives Created by the FCPA's "Reason To Know" Clause:

- (1) The U.S. Embassy in Muscat, Oman reported that a U.S. firm lost a \$20-\$30 million contract solely because of the time delays needed to investigate sales agents and assess their responsibility for third parties under the FCPA.
- (2) A multinational U.S.-based engineering company spent approximately \$250,000 to evaluate its potential market in Latin America. Brazil, Mexico, and Venezuela were considered open markets for exporting engineering services and establishing local service branches. One of the major reasons the company chose not to expand was its uncertain liability under the FCPA for the activities of independent agents and subcontractors. Moreover, the cost of policing such activities would have markedly lessened its price competitiveness.
- (3) In Oman, a large Utah firm has encountered difficulty over the past couple of years in its efforts to obtain a local representative. After many discussions, the U.S. company narrowed the field to one Omani firm which it felt could best represent its interests, but the Americans have been unable to reach an agreement due to potential problems arising under the FCPA. Since the firm's business runs in multimillion dollar contracts involving proprietary technology, lost U.S. exports may have been substantial.
- (4) In Liberia, U.S. firms will not risk hiring local agents because of potential liability under the FCPA for their unsanctioned actions. Instead, they have come to rely on more expensive expatriates with fewer ties to local business people. Not only has the cost of doing business in Liberia gone up, U.S. firms have lost their competitive edge.

- (5) The U.S. embassy in the United Arab Emirates reports that overlap between business and government has been a problem for U.S. firms seeking to do business there. At best, the overlap has made it more difficult for U.S. firms to begin operations -- in many cases months pass while home office legal staffs review potential sponsorship agreements. Some firms have signed relatively ineffective agents rather than violating the FCPA, or at worst, have decided not to enter the market at all. At the same time, the U.S. image in the host country suffers, because many reputable businessmen resent what they perceive as a questioning of their own honesty in business dealings.
- (6) In Qatar, only one of the state's 14 cabinet ministers has no known business ties, and U.S. firms often fear that business payments may be construed as illicit payments to foreign officials. American firms there generally avoid agents in government positions, but they are then restricted to less effective agents with fewer business connections throughout the region.

-- Increased Costs and Lost Trade Generated By Confusion Over What Constitutes a Facilitating Payment:

- (1) The local director of an American company in a foreign country paid a customs official \$20 to process the release forms for spare parts to a broken machine; the official suggested that the alternative would have been to wait several days for "further formalities." According to the FCPA's legislative history this should have been a legal payment, and the local director was reimbursed by his managing director in the U.S. Because of uncertainty over what constitutes a facilitating payment, however, the payment did not pass the internal auditor from the home office. The American managing director's career is now on the line, and the parent company has spent \$30,000 internally investigating why the \$20 payment was made and how to cope with it under the FCPA.

- (2) During a trip to Singapore, a U.S. company learned that a series of payments would be required in order to do business in Indonesia. These included payments to the switchboard operator in the hotel, to secretaries for arranging appointments, to the administrative assistant of the customer to meet with the customer, to all company sales representatives, to guards watching unloaded merchandise, and to customs officials. Unclear as to which payments were prohibited by the FCPA, the company did not compete to install communications equipment.
- (3) Since Brussels, Belgium is the headquarters for many companies which do business in Africa and the Middle East, the U.S. embassy there detected that American firms avoid export opportunities which corporations from other countries do not hesitate to undertake. A U.S. construction firm, for example, was interested in bidding on a project in a Middle Eastern country where facilitating payments are both customary and necessary. Unwilling to confront the FCPA's ambiguous definition of facilitating payments, the firm decided to be a subcontractor for a European prime contractor and accept a much smaller portion of the project.

-- Consequences of Failure to Follow Customary Business Practices in Foreign Markets:

- (1) In China, a U.S. firm had concluded a \$4 million contract for the supply of construction equipment. The American firm, overzealous about enforcing the FCPA, then refused to pay legitimate commissions to a Chinese distributor because of technical delays in obtaining receipts from the Bank of China. The Chinese distributor revoked the contract and purchased the construction equipment from a Japanese firm that was willing to pay the commission.
- (2) In Thailand, it is normal practice to "assist" government officials through cash payments, gifts, free travel, etc. A U.S. office equipment company, concerned about potential FCPA violations, refused to "assist" potential customers. In one case of lost business, the U.S. firm obtained the bid documents. Had the company made the requested payments, its bid would still have been 15 to 10 percent lower than the Japanese firm which won the contract.

- (3) A U.S. company had been considering setting up wholly-owned marketing companies in countries such as the Phillipines, Indonesia, Thailand, South Korea, and Taiwan to replace local sales agents. In light of local customary business practices, these plans were deferred indefinitely because of excessive expenses for ensuring compliance with the FCPA.

-- Negative Foreign Response to the FCPA:

- (1) A large American firm was pursuing a joint venture agreement with a reputable Saudi firm. In order to protect itself from the unknowns of the FCPA, the U.S. firm insisted on protective language in the contract. The Saudi firm was offended by inferences that its officers were corrupt and delayed the negotiating process. Meanwhile, a third country firm received a lucrative contract from the Saudi Arabian government which had been tentatively awarded to the partners-to-be. The joint venture may never be worked out because of the bad feelings which were generated in the contract negotiations and due to the loss of the contract.
- (2) In another case, one American and one Saudi firm were engaged in negotiations concerning an industrial joint venture involving more than \$100 million in capital. Because of the large amount of money involved, the American company insisted on a buy-out clause which it tied to the FCPA. The Saudis, however, could not accept the provision because they felt that the FCPA was vague and feared that the U.S. firm could pull out and demand compensation at any time by claiming that the law had been broken. Although negotiations continued for several months, the joint venture never materialized.
- (3) An American steel company which was negotiating a cooperative venture with a Chinese corporation refused to pay for travel expenses in the U.S. during a planned trip by the Chinese executives to inspect the American company's facilities. Offended by the American company's refusal to pay under the FCPA, the Chinese executives never visited the U.S. and cut off contract negotiations.

- (4) An American company held 20 percent equity in a company in Southeast Asia. Under a consent agreement reached with the U.S. government, the manager of the American company was required to sign quarterly statements of FCPA compliance. The board of the foreign company requested that the U.S. firm either replace the American manager with another national who would not be required to sign the compliance statement or divest their interest in the company. Since a change of manager would not release the American company from the FCPA compliance agreement, they were forced to divest. The losses for 1979 on the investment, management fees, and profit sharing were estimated at \$2 million.
- (5) A European consortium received a foreign contract for an amount 333 percent greater than the U.S. company's preliminary bid. The U.S. company believes the prospective customer did not want to deal with a company subject to the FCPA.

-- Lost Business Arising From U.S. Firms Withdrawing From Existing Markets:

- (1) A U.S. firm in Cameroon withdrew its bid for a \$15 million television contract when several European firms entered the competition. The firm simply did not want to compete for the contract because it felt the FCPA might become an issue.
- (2) In Haiti, no U.S. firm has competed for any of the major projects undertaken in the last 18 months. These included: a sugar mill worth \$45 million, a vegetable oil refinery costing \$12.5 million, a new fishing fleet priced at \$16.6 million, and a contract for a new bus fleet worth \$2 million. The U.S. embassy there speculated that the FCPA was the major disincentive to competition.

Mr. WIRTH. Did the U.S. Trade Representative or your staff compile the examples of problems that you are referring to in this document that has just been inserted in the record?

Mr. BROCK. Most of these came out of the survey from the embassies around the world. I was going to cite this example No. 6, which was the first one you saw, the embassies in Oman reported, because it is so common for prominent Omani businessmen to also hold government office, and that is true in a lot of the developed world, the FCPA cause special problems.

Of major firms, only a handful have firms among the principals. U.S. companies seeking local representation then as required by Omani law often find that the few Omani firms not owned by government officials already represent their U.S. competitors or competitors from other countries around the world, so they are faced with an impossible dilemma.

They either hire a representative of government, and that is in violation of the law, which they can't do, or they hire a firm that is not related to government, but that firm is representing their competitor. They are caught. What do they do?

Mr. WIRTH. As long as we are on this documentation which has been used extensively, let's take a very careful look at the documentation that we just included in the record. It was submitted on the Senate side and submitted as part of your presentation to us. If we look very carefully at this, at least seven of the examples that were used by USTR came from a report prepared by the chamber of commerce entitled, "The Price of Ambiguity."

I assume that you got that information from the chamber.

I don't know if it is clear to people how the chamber got its information. We talked to them and asked them how they got it. They told us that the chamber had asked for examples from business of their problems under the Foreign Corrupt Practices Act for the purpose of building a case to amend the act.

They got some 180 replies and selected a handful of examples out of those 180 which became part of this document.

The examples in the report in many cases were unclear. It is difficult to tell, looking at the history of how this evidence was put together, just what companies wished to do that they believed they could not do under the act.

I don't know if anybody has gone about verifying this or has just taken that information in from the chamber. Do you know if any of the examples used among the 19 that came from the chamber were verified? At least seven came from the chamber. Do you know if they were verified?

Mr. MARONI. The chamber is able to report that.

Mr. WIRTH. You say the chamber has that information. We asked the chamber if they have that information. Mr. Brock's staff says the chamber has that information.

The first response was that the information was confidential and could not be given to the Congress. We pressed on that, and then we were told that in fact the documents had been destroyed.

It is a little bit difficult to put a lot of faith in these examples, and I would say that those examples are of little probative value. To talk about the evidence, let's go on to the other 12 or so examples that came from the Department of State.

At this point, I would like to put in the record a copy of the cable that was sent to U.S. Embassies. The outgoing cable explains that the administration was concerned with the Foreign Corrupt Practices Act.

Without objection, the full cable will be included in the record.
[The cable referred to follows:]

UNCLASSIFIED
Department of State

OUTGOING
TELEGRAM

PAGE 01
ORIGIN ED-01

STATE 134954

5912

STATE 134954

INFO OCT-00 AOS-00 INR-10 EOP-10 AF-10 CDR-00 EA-10
N-01 10-10 NEA-01 SEC-01 OPA-10 NSAT-01 OEP-10
L-01 TAGE-00 PCN-00 STR-10 JUST-00 SP-01 /115 R

CREATE PROBLEM IN FOREIGN RELATIONS AND CUTS DOWN EXPORTS.
WE ANTICIPATE FURTHER HEARINGS ON THE COMPANION HOUSE BILL,
H.R. 2530, WHICH IS IDENTICAL IN ITS TERMS TO S.708.

5. IN VIEW OF SENATOR HEINZ' REQUEST FOR SUCH INFORMATION
AND RELEVANCE OF SELECTED INFORMATION TO LATER HEARING,
WE WOULD APPRECIATE BEST AVAILABLE INFORMATION FROM POSTS
BY JUNE 2 ON FOLLOWING POINTS:

- (A) DETERMINANT EFFECT OF FEPA, IF ANY, ON BUSINESS -- CAN
YOU CITE CONCRETE EXAMPLES WHERE FEPA DISCOURAGED U.S.
FIRMS FROM BIDDING ON CONTRACTS OF WHERE U.S. FIRMS LOST
OUT TO FOREIGN FIRMS BECAUSE OF AMBIGUITIES OF PRESENT
ACT? WE DO NOT HAVE IN MIND UNRESTRICTED BRIBERY COMPE-
TITION, RATHER WHETHER U.S. FIRM MIGHT HAVE DONE BETTER
WITH FEPA MODIFIED ALONG CHAFFEE LINES?
- (B) EMPHASISMENT TO FOREIGN OFFICIALS -- CAN YOU CITE
EXAMPLES WHERE THE EXTRATERRITORIAL REACH OF THE ACT HAS
OR MAY HAVE CREATED FRUSTRATIONS IN BILATERAL RELATIONS?
- (C) ANY OTHER COMMENTS.

6. EXAMPLES SHOULD BE UNCLASSIFIED BUT PLEASE PROVIDE
CLASSIFIED PARAGRAPHS, IF NECESSARY, TO PLACE IN CONTEXT
OR ADD FURTHER DETAILS.

7. PLEASE CITE SOURCE NUMBERS OF PREVIOUSLY REPORTED
MATERIAL, NAIG.

NOTE BY DEPT: POUCHES KABUL AND BEIRUT.

P 230100Z MAY 81 ZEN
FM SECSTATE WASHDC
TO ALL DIPLOMATIC POSTS PRIORITY
KABUL POUCH
BEIRUT POUCH

UNCLAS STATE 134954

E.O. 12065: U.S.

TAGS: ETRD; BEIP

SUBJECT: FOREIGN CORRUPT PRACTICES ACT (FCPA) -- S. 708,
-CHAFFEE AMENDMENT

1. ON MAY 20, USTR, COMMERCE, STATE, AND JUSTICE TESTIFIED
ON THE CHAFFEE AMENDMENT (S. 708) TO SIMPLIFY FEPA, BEFORE A
JOINT HEARING OF THE SUBCOMMITTEE ON INTERNATIONAL FINANCE
(HEINZ) AND THE SUBCOMMITTEE ON SECURITIES (D'ANATO) OF
THE SENATE COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
ADMINISTRATION WITNESSES, LED BY BROOK OF USTR AND INCLUD-
ING JOHNSTON OF STATE DEPT, PROVIDED STRONG SUPPORT FOR THE
BILL, ALTHOUGH SUGGESTING SOME CHANGES. QUESTIONING BY
HEINZ, D'ANATO, AND CHAFFEE, PREDICTABLY, WAS FRIENDLY,
WHILE PROHIRE, AUTHOR OF 1977 LAW, RAISED STRONG OBJECTIONS.

2. IN ESSENCE, CHAFFEE BILL SEEMS TO REMOVE AMBIGUITIES OF
FEPA BY, INTER ALIA: (A) CLARIFYING RELATIONSHIPS BETWEEN
U.S. PRINCIPAL AND AGENT -- CONCEPT OF "REASON TO KNOW"
WOULD BE REPLACED BY REQUIREMENT THAT U.S. PRINCIPAL DIRECT
OR AUTHORIZE PROHIBITED ACT BEFORE U.S. PRINCIPAL WOULD
BE CULPABLE FOR ACTS OF AGENTS. (B) LIBERALIZING
EXPEDITING OR FACILITATING ("GREASE") PAYMENTS TO TAKE INTO
ACCOUNT LOCAL CUSTOMS. (C) PERMITTING PAYMENTS IF LAWFUL
IN COUNTRY WHERE MADE. (D) SIMPLIFYING ACCOUNTING PROVISIONS.

BY USE OF "MATERIALITY" STANDARD AND (E) CENTRALIZING
ANTI-BRIBERY ENFORCEMENT IN THE JUSTICE DEPARTMENT, REMOV-
ING SEC FROM THAT AREA. MOREOVER, S. 708 EMPHASIZES ADMINI-
STRATION TO CONTINUE EFFORTS TO REACH INTERNATIONAL AGREE-
MENT ON ILLEGIT PAYMENTS.

3. AMONG CHANGES SUGGESTED BY ADMINISTRATION WAS THAT
ACCOUNTING PROVISIONS OF CHAFFEE BE DROPPED WITH SUBSTITU-
TION OF SIMPLE, GENERAL PROVISION FOR CRIMINALIZATION OF
FRAUDULENT RECORD KEEPING DESIGNED TO CONCEAL ILLEGIT PAY-
MENTS.

4. ADMINISTRATION WITNESSES, INCLUDING DEPARTMENT, MADE
CLEAR THEIR VIEW THAT INTENT OF S. 708 IS NOT REPEAT, NOT
TO CUT FEPA -- BRIBERY OF FOREIGN OFFICIALS WOULD STILL
BE CRIMINAL OFFENSE -- BUT TO LESSEN UNDESIRABLE CONSE-
QUENCES OF ACT. IN DEPARTMENT'S VIEW, EXISTING LAW CAN

UNCLASSIFIED

Best Available Copy

Mr. WIRTH. It says the following.

On May 20, USTR, Commerce, State and Justice testified on the Chafee amendment, S. 708, to simplify the Foreign Corrupt Practices Act. Administration witnesses provided strong support for the bill, although suggesting some changes.

In essence, the Chafee bill seeks to remove ambiguities of FCPA. In the department's view, existing law can create problems in foreign relations and cuts down exports. We would appreciate information from posts on the following points: (a) deterrent effect of FCPA, if any, on business; (b) embarrassments to foreign officials—can you cite examples where the extra territorial reach of the act has or may have created the irritations in bilateral relations; (c) any other comments.

One asks, reading this, why weren't any of these posts simply asked to comment on the foreign trade impact of the FCPA. Why was the telegram prefaced with the administration's negative views of the act. Why were the negative responses the only ones that were solicited, and why weren't any positive reactions asked for?

Maybe the State Department could have gone out and asked where the Foreign Corrupt Practices Act has been a very positive thing for U.S. trade. Maybe the act has created faith and trust in relations with other countries. Give us examples of that as well.

Again, those are the other 12. There are 19 examples in this document. At least seven came directly from the chamber, unverified documents that were destroyed. The others came from the cable that went out, which tell us all the problems with FCPA prefaced with the administration's statements that they wanted to amend the FCPA.

Now, if you are a lower level bureaucrat in the State Department responding to that kind of a cable, what are you going to do when the administration says it is our intent to change the act, we support this piece of legislation and give us examples as to how to do it? You are going to respond and send in everything you can.

I would do that, being a responsive, good civil servant, working in the State Department. Mr. Rinaldo, I thank you for bringing that up.

What I wanted to do was to clarify exactly what it is we are dealing with in the data and make sure that the record shows that very clearly. I have impinged upon the gentleman's time.

I just wanted to point out that if there are ambiguities, let's look at the ambiguities, but again, let's not paint it with a whole lot of other suggestions about its relationship to overall trade and imply that the evidence is strong and clear.

Mr. RINALDO. Mr. Chairman, we also have to recognize that there may be very good reasons why some companies wouldn't want their names bandied about and headlines telling about the business they lost and the reasons why they lost it.

Quite frankly, while we are looking for evidence—I have only been here 9 years, so maybe I am still a rather young Member of Congress—I haven't seen a piece of legislation yet where the evidence was any more overwhelming than what has been presented here thus far.

If we are going to worry about evidence that reaches the ceiling of this hearing room, then quite frankly we wouldn't pass a piece of legislation on the floor. Yesterday the majority on the floor, in many cases with the aid of the minority, rammed through a lot of legislation without any evidence whatsoever.

All you have to do is read today's paper, or any paper in any major city in this country, and you will know what happened on the floor of the House yesterday.

Mr. WIRTH. Mr. Rinaldo, it is not your responsibility, nor my responsibility as a member of this subcommittee, to do a sloppy, unthoughtful and "nonhomework" job in any legislation, whether it is the international communications bill, the rewrite of the Communications Act of 1934 or this legislation.

The fact that there may or may not be sloppy workmanship elsewhere in the institution does not sanction that on this subcommittee as long as I am the chairman of the subcommittee.

Mr. BROCK. Mr. Chairman, it is equally valid to say that you may not like what someone else says. You may discredit the testimony of one particular individual, but that does not itself remove the Congress responsibility of dealing with what in fact is a law that is generally accorded negative rulings by the business community.

As Dan Mica said, you either have to believe that there is a conspiracy among the entire American business community worldwide and they found some form for getting together without us knowing about it so that they all say exactly the same thing, that this bill is an impediment to their ability to compete, or you have to say that there is an enormous body of evidence that says that something is wrong and the thing ought to be cleaned up.

Mr. WIRTH. Mr. Ambassador, we are just looking for the information. We know the only documented information we have, a survey that has been looked at, is the GAO report, in which two-thirds of the people responding to that report—and it has got all kinds of problems, too, it is anecdotal—said there no problems. We do not have coming in, in all the documents submitted on the Senate side, and submitted over here, a clear trail that suggests that there are very big problems.

We have never asked of the business community or of our embassies overseas anything positive about this legislation. The burden has been to say we believe this is wrong, whether it is the chamber of commerce's questionnaire going out or it is the State Department's cable. We believe that there are significant problems in this legislation. Tell us what those problems are. The other side has never been looked at at all.

Mr. COLLINS. Mr. Chairman, I have talked to businessmen in my area quite a bit. We do a lot of trading in our area, and I have not heard one single soul say a good word on behalf of this law. I think if the gentleman spends a few days when he is back in Denver during the holidays, he is going to be surprised at how many negative words he can get.

I don't know whether you do any export business back there in Colorado or not—everybody goes there for skiing in the winter, I don't know what they do the rest of the year—but I have never heard one—

Mr. WIRTH. If the gentleman will yield.

Let's keep to the very specific focus on the reality of this legislation and what it does and what it doesn't do.

As the gentleman knows, we are deeply involved in all kinds of export business. There is not an overwhelming groundswell of people pouring over the transom in my office in Colorado or here

saying that this is the worst thing that ever happened or the greatest inhibition around.

Businesses in my area are much more concerned about what is happening to the value of the dollar. They are much more concerned about oil imports into this country. They are much more concerned about the decline of research and development. They are much more concerned with the fact that we are cutting off language training and area studies.

Those are areas that are of much, much greater concern in any kind of listing related to foreign exports in the country than is this piece of legislation.

Now, occasionally people mention it, but there are other things that rank 1 to 10 far ahead of this. It is suggested not only in the anecdotal evidence that I get, but a recent conversation with Mr. Bergston about the Foreign Corrupt Practices Act that the act ranks way below a whole lot of other variables as well.

So, I think let's keep an eye on what is important and what isn't important in looking at the whole export situation.

Mr. COLLINS. I thank the gentleman.

I would say in my area jobs are the most important thing. Business people think we have too much government. When you talk to them about more government and more regulation, they will all say let's modify these regulations.

The chairman just mentioned that we should work to improve sloppy legislation. I think this law itself, when it was conceived, represented sloppy legislation.

I will tell you an example I heard about. I wasn't looking for it. I just picked it up from a guy who sat next to me on the airplane.

He told me about a deal he lost—it wasn't a big deal, but \$10 million is a big one to him—in the Middle East because the company over here said they thought that the agent that had developed the business knew somebody over there. He said the company thought he was as clean as can be. I said, why did they back out? He said they were afraid, because of this law. I said, well, who got it? He said that the agent took it over and gave it to the Germans.

What I want to ask is this. Does any other country in the world have a law like the Foreign Corrupt Practices Act?

Mr. BROCK. Not as we have it, no.

Mr. COLLINS. How many of them have this type of legislation in different forms?

Mr. BROCK. I don't know of any other than Japan that has some form of bribery law, but it is pretty much in consonance with that applied domestically. They don't try to extend that internationally.

Mr. COLLINS. That is the big point. Repeat that. The normal practice is to use the domestic law. Instead, we are putting a double burden on our businesses when we get into foreign trading. So we really are discouraging American businessmen from it.

Now, what specific provisions of the law do you think have been the most responsible for loss of export business?

Mr. BROCK. The definition relating to reason to know, which is almost impossible to understand the accounting provisions in conjunction with one another, leave an uncertainty of application that has caused an enormous problem.

I was just handed a note to say that no other country has an extraterritorial FCPA.

Mr. COLLINS. Not another country in the world?

Mr. BROCK. That is right.

Mr. COLLINS. In other words, we are setting ourselves up to handicap our business when no other country does. I just looked at TV as I came in this morning, and automobile sales are hitting an all-time low.

Incidentally, how many automobiles do we sell to Japan? What percentage of their market do we get?

Mr. BROCK. Considerably less than one-tenth of 1 percent.

Mr. COLLINS. And yet today we are hitting an all-time low. Everywhere we go, it is not the Arabs alone. We are finding this in every market. Let me come back to the reason to know standard. That concerns me very much. Do we have that standard in our domestic bribery law?

Mr. BROCK. No, sir.

Mr. COLLINS. Not in any way?

Mr. BROCK. No.

Mr. COLLINS. Do you know from the history of the law why we have the reason to know clause?

Mr. BROCK. I think people were so excited about the Lockheed scandals and others that were similar that they wanted to write a quick law. I think they drafted it with very good intent, but perhaps without adequate care.

Frankly, I don't know how you predict what these laws are going to do until you try them for a while. We tried it for 4 years and we found a problem. That is why we are up here to suggest that modification might be worthwhile.

Mr. WIRTH. If the gentleman will yield on the "reason-to-know" issue, is that unique to the statute?

Mr. BROCK. I think you will have to ask the lawyers. Maybe Justice can respond to that better than I.

Mr. WIRTH. There is a long history of the "reason to know" provision. It appears in 29 other Federal criminal and civil statutes.

Mr. BROCK. I am glad I didn't answer the question because you knew the answer when you asked it.

Mr. WIRTH. That is right. I just think we ought to understand. Does that suggest that we ought to go back and amend all those 29 other statutes as well?

Mr. BROCK. Maybe those were written with more care and in a different context so that it could work.

Mr. COLLINS. Since we are putting all of this in the record, we are talking about domestic bribery law, and as I understand it, we don't have it in domestic bribery law.

Where does this reason to know standard come up?

Where is it found in other laws, just for the record right now, since the chairman raised it? Where do we have all this reason to know responsibility on business? Is it on business?

Mr. BROCK. It probably refers to Government officials. They seem to be more guilty of corruption than others, recently.

Ms. COCHRAN. We have one on civil disorders, another on confiscation of wire communications, and interceptions of wire communications.

This data, for your information, Congressman, has come from Mr. John Fedders, who is the Director of the Division of Enforcement at the SEC. He did an article on the "reason-to-know" standard, which we included in the record at the last hearing, and he cited 29 examples.

Now, we haven't gone through all of them, but he did give the actual statutory citations for all 29 of those statutes.

Mr. COLLINS. Did he quote in there what our requirements are compared to foreign law? In other words, this looks to me like it is just a harassment feature that we have put in to try to handicap American business. Did he quote what the foreign statutes were?

Ms. COCHRAN. No, he didn't, not on "reason to know," but he did point out that it does exist in 29 Federal criminal and civil statutes.

Mr. RINALDO. Do any of them you are citing presuppose that a person will have a reason to know the actions of an agent in a foreign country so that it can be linked with this particular law?

Mr. BROCK. I think that is the basic point. This is an extraterritorial application.

Mr. WIRTH. Mr. Fedder's piece is in the record of the last hearing. Again, the purpose of raising this is that the "reason to know" provision was not one that is unique to this act. It is one that exists in lots of other places.

Mr. BROCK. It is unique, Mr. Chairman, in the extraterritorial application. It is the only law that we know of in which know or reason to know is used in that extraterritorial application.

The problem with that is that it is far more difficult when you are dealing with agents and agents of agents, where you can be put into jail for 5 years and find thousands or millions of dollars, it is a far difficult and complicated subject in an extraterritorial application.

Mr. COLLINS. I think the reason to know is the most important feature that ought to go. That is one that is just impossible to live with abroad.

Mr. BROCK. May I just interject, Mr. Chairman, I really am running out of time, and I apologize, but I think you are in an area where other people have more expertise than I, and I would hope that—

Mr. WIRTH. Perhaps you might have time for Mr. Rinaldo, who has been especially concerned with this piece of legislation. We have all impinged upon his time.

Mr. RINALDO. Yes, I think we have certainly kept the Ambassador here long enough. I do want to thank you for your testimony. It is obvious that you have a great deal of knowledge about the effect that the Foreign Corrupt Practices Act has had on our exports.

I would just like to ask one question that I think is particularly important because, while we are looking for evidence other than anecdotal evidence, it should also be put into the record that the Carter administration listed this act as a major export disincentive.

The Senate Banking Committee passed a bill by an 11 to 4 vote. The entire Senate passed the bill by a voice vote. There is bipartisan cosponsorship in the House, and when we talk about exports or export opportunities that are lost because of this act, and the effect of the act, what we are talking about is lost American jobs.

Yesterday at a meeting I was at, people said that is the number one issue in the country—jobs. We need more jobs.

Can you give us any information—and if you don't have it here, perhaps submit it for the record—about how many jobs are lost with the loss of, for example, a million dollars in export business?

Mr. BROCK. It varies so much by product line. Agriculture, for example, is very productive and has a very low labor content, so the jobs lost in agricultural sales would be less than those lost in the heavy manufacturing sales, for example. Generally the figure has been used of about 40,000 jobs per \$1 billion.

Now, the reason I wanted to mention that is because I think your point is so valid. The emergency committee, ECAP, submitted testimony when they surveyed just their own membership—not all industry, just their own membership—that they had lost \$2 billion worth of jobs in those companies alone, just due to the lack of understanding of the law.

They are not talking about failure to have the right to bribe. They are just saying the complexity, the ambiguity alone costs \$2 billion.

Now, the chairman keeps asking for a number. That is one, and it is hard; \$2 billion is 80,000 jobs. Some people say, well, it is only \$2 billion. Tell those 80,000 people that it is only 80,000 jobs and you will get a different answer. It does have an impact.

Mr. RINALDO. I don't want to keep you any longer. I will just ask one more question that naturally flows from your response.

Mr. BROCK. 8,000, I am sorry. I will correct it if I need to later.

Mr. RINALDO. Because of some of the considerations, American companies have to take into account in doing business with foreign governments because of the FCPA, what uncertainties are they dealing with that cause them to, in effect, hold back as a result of this statute? What are the major uncertainties? Can you describe some of the considerations?

Mr. BROCK. Yes. We tried to do that in the examples we submitted. I don't call them anecdotal. We just have a different definition of what an anecdote is. I mentioned the company or the companies that tried to operate in Oman, where almost all of the representation businesses—and you have to, under Omani law, do business through their firms—most of those firms have as allowable under Omani law Omani officials.

Now, under the lawyer's interpretation of this bill, you couldn't do business with those firms because government officials are involved. If you seek an Omani firm that doesn't have a government official involved, they are already doing business with some germane competitor you have got or Japanese competitor.

That is one example where there is really no place left to go.

Another example. A firm wanted to have a business partnership with a firm overseas and they invited our business people over there. They paid their expenses, flight, hotel, meals. Our business people went over there. They had good meetings.

Our people invited them back, and all of a sudden the lawyers said you can't pay their way back as they paid yours. So we had to say we can't do it. We can't bring you back to the States to conclude the conversation, so we don't have the joint venture operating.

I mean, there are just hundreds of those things that are happening all around the world, and I don't know how to quantify that. We have tried with some illustrative cases that are factual as far as we know to demonstrate the kind of problems, but the basic thing is that our people don't know whether you are dealing with a functionary or an official.

They don't know, what do you mean know or reason to know. What is the reason to know? Define that for them. They go to Justice. They can't get an answer unless they go with a specific case, but they don't know what the case is until they go out and try to get the business.

They go to the SEC. They can't get any answers. They have got two different agencies. The Accounts Association of the United States has given them one set of criteria for compliance with the law.

The lawyers, the Bar Association, have given a different set of criterial They get a different set of criteria from the SEC. Those are three groups each telling of different ways to comply with the law.

That is the problem. It is driving them up the wall. What they have done is to say we are just going to stop trying to do business in Southeast Asia, we are going to try to stop doing business in the Middle East, and we are not doing business there. We are not competitive there.

Now, if you can tell me how to quantify that and give you specific cases of business we haven't gotten because we are not even competing over there, I don't know how to do it, but I can tell you that they have withdrawn.

Mr. RINALDO. It is difficult to quantify things of that nature, but certainly your testimony reveals that based upon your own experience, your own discussions, your own meetings with foreign officials, it indicates that this legislation as currently written is a major impediment to United States companies that are in the business of exporting.

Mr. BROCK. Absolutely.

Mr. RINALDO. Thank you very much.

Mr. BROCK. Thank you.

Mr. RINALDO. I appreciate your testimony.

Mr. WIRTH. Mr. Tauke?

Mr. TAUKE. Thank you, Mr. Chairman.

Mr. Ambassador, from the vantage point of this member, you are doing a very fine job in your position as Special Trade Representative. I know your time is limited, so I will not pursue the matter with questions.

I do have to say, however, that I do think that our subcommittee is doing some disservice in not moving more quickly on this legislation. I have great respect for the chairman. I think he does a superior job of thoroughly studying information and thoroughly studying legislation before it is adopted, but in this case I fear that we are pole vaulting over anthills when it comes to trying to develop evidence.

There are some things where evidence is obvious to those who want to see. Yet, it is very difficult to quantify.

I do hope that you and your people do all you can to try to get us the best evidence that you can, because we apparently are going to need that. I want you to know that there are some of us who are very committed to seeing that this legislation does move.

Mr. BROCK. Thank you very much.

Mr. WIRTH. I thank the gentleman.

Mr. Ambassador, thank you very much for being with us. I greatly appreciate your longevity here and your patience. I appreciate it.

Mr. BROCK. Thank you.

Mr. WIRTH. Our final two witnesses are Mr. Ernest Johnston of the Department of State and Mr. Sherman Unger, General Counsel of the Department of Commerce.

Gentlemen, thank you very much for being here. Would you introduce yourselves, please, for the reporter. I think you know the rules of the subcommittee, requesting that you summarize your statements. Your statements will be included in full in the record, and we will then have the opportunity of exchange with you.

Contrary to a lot of conventional wisdom, Members of Congress can read, and we will look at those statements when they are in the record.

STATEMENTS OF SHERMAN E. UNGER, GENERAL COUNSEL, DEPARTMENT OF COMMERCE; AND ERNEST B. JOHNSTON, JR., DEPUTY ASSISTANT SECRETARY FOR ECONOMIC AND BUSINESS AFFAIRS, DEPARTMENT OF STATE

Mr. UNGER. Mr Chairman, I am Sherman Unger, the General Counsel for the Department of Commerce. I would ask that my prepared statement be submitted.

Mr. WIRTH. It will be included in full in the record.

Mr. UNGER. I doubt even if my summary can add anything to the testimony and exchanges that have taken place so far this morning. I have a couple of comments that I would like to make.

I understand you are interested in statistics and hard evidence. I appreciate that. However, I think we are dealing in an area in which it is difficult to measure those companies that have not participated because their counsel did not feel competent to render a decision interpreting the law as it is presently written.

Having recently left the private practice of law, and being fully aware of the malpractice suits, what happens is that the lawyer that renders an opinion becomes an insurer, and this is a very difficult law to render an opinion on. It is vague; it is uncertain.

I have a single experience, if I may talk about my own experience, in which I tried to write an opinion. My final analysis was "you had better stay out of it," and my client did.

He was a small manufacturer in the Midwest. It was just a marginal increase in his productivity, and it seemed the wiser advice to tell him, "It is a very vague law. I can't write you an opinion that will make you comfortable. I don't think you ought to venture into export trading," and he did not.

I would, since I am a lawyer and Ambassador Brock is not, appreciate an opportunity to refer at greater length to Mr. Fedder's

article, the title of which is "The 'Reason to Know' Standard—A Troublesome Ambiguity in the Foreign Corrupt Practices Act."

I would, if I may, like to refer to Mr. Fedder's article in which he states that the standard appears in 29 provisions of Federal, criminal, and civil statutes. "The statutes containing the provision and the case law interpreting it do not provide a satisfactory definition."

He continues by saying, "Reason to know implies no duty of knowledge on the part of an actor." I will read from a couple of paragraphs in that same article that I would like to put in the record:

Under the standards a U.S. businessman arguably could be required to review all of the facts surrounding each proposed sale to a foreign government to guard against the possibility that later charges might be made that there was "reason to know" of a prohibited payment.

He continues:

Moreover, when lawyers and businessmen have conducted a review of facts to satisfy themselves that circumstances do not give rise to reason to know, the results have been inconclusive, often leaving withdrawal from the transaction as the only safe course of action.

I would only like to quote from a footnote on the definition of reason to know, where Mr. Fedders says in part:

Moreover, the foreign context is the least fair of all situations in which to apply a "reason to know" standard. Although such a standard might be appropriate in statutes which govern conduct in the U.S., where the circumstances from which "reason to know" could be inferred are familiar both to those subject to the law and those enforcing it, such a standard is unfair when applied to conduct in foreign countries where the language, laws, customs and practices are different from those in the U.S. and vary greatly from one country to another.

Reason to know is vague. Reason to know is not definitive. Reason to know is subject to second guessing.

I submit that there is a great body of business not conducted because corporations are afraid of the statute and their lawyers are reluctant to write an opinion on a statute that is so difficult to assess and measure.

Thank you.

[Mr. Unger's prepared statement follows:]

STATEMENT OF SHERMAN E. UNGER, GENERAL COUNSEL
DEPARTMENT OF COMMERCE
BEFORE THE SUBCOMMITTEE ON TELECOMMUNICATIONS
CONSUMER PROTECTION, AND FINANCE OF THE HOUSE COMMITTEE
ON ENERGY AND COMMERCE
DECEMBER 16, 1981

INTRODUCTION

Mr. Chairman and Members of the Subcommittee:

I am pleased to participate in today's oversight hearings on implementation of the Foreign Corrupt Practices Act (FCPA).

My testimony will follow up on Ambassador Brock's statement and relate his overall remarks about the FCPA as an export disincentive to specific sections of the Act which are of particular concern to the business community.

My prepared statement is brief: I shall limit my remarks to a summary of the principal problems which have been mentioned in implementation of the FCPA and ways in which we feel it can be improved. I anticipate also that the Committee may want to leave time to explore further the information previously submitted in response to the Chairman's request.

At the outset, I want to emphasize a point made by Ambassador Brock in his testimony. This Administration agrees with the underlying purpose of the FCPA and believes that bribery and corruption in international business transactions is inherently wrong.

In advocating revision, we are merely recognizing that this Act, like other statutes, should be examined periodically to ascertain how well it is working. The Act is four years old, and we now have enough experience with it to see that some changes are necessary in order for the Act to serve its intended purpose and not operate as an export disincentive.

The business community has identified three major problems with the current law that we believe need resolution if the U.S. is to increase its exports. They are: (1) imposition on a corporation or individual of liability if there is "reason to know" that a payment is illegal; (2) the presence of burdensome and costly accounting provisions; and (3) confusion over what types of payments are permissible under the Act. I shall deal with each of these in turn:

"REASON TO KNOW" STANDARD

Corporations have consistently said that the vagueness and ambiguity over when "reason to know" exists has deterred them from involvement in otherwise lucrative overseas opportunities because of a fear that they would be charged with an FCPA violation.

For example, in September, 1980 the Report of the President on Export Promotion Functions and Potential Export Disincentives identified the "reason to know" standard as the Act's principal disincentive.

In December, 1980, the Report of the President's Export Council also listed the standard as a major disincentive, and the March, 1981, GAO report on the FCPA reached the same conclusion.

The "reason to know" standard is particularly troublesome for a corporation that hires an agent who then without authorization bribes officials. In that case, a corporation can be found liable by a court in hindsight making a subjective judgment that a company should have known of the agent's conduct.

In one case that has previously been disclosed to the committee,^{1/} a U.S. firm lost a \$20-30 million contract because of time delays caused by investigating the reputation of various agents and assessing potential corporate responsibility for their actions.

In Latin America, another company spent approximately \$250,000 in an effort to expand its export market but decided against expansion because of potential liability under the "reason to know" standard.^{2/}

In our judgment the purposes of the FCPA can be met without interjecting such a vague and ambiguous standard. We believe the approach taken by the Senate in S. 708, whereby liability under the Act comes from payments "directed or authorized" by a corporation, is an appropriate solution.

The "direct or authorize" standard serves clear notice that corporations will not be able to order bribery of foreign officials and also relieves companies from the apprehension that they will be held liable for activities for which they were not responsible.

^{1/} "Examples of Lost Trade and Increased Costs Created by the FCPA," Office of the United States Trade Representative (Attachment A to the materials submitted previously to Congressman Wirth), at para. 1.

^{2/} Id., at para. 2.

ACCOUNTING PROVISIONS

We believe that the Committee should strongly consider replacing the accounting provisions in Section 102 of the FCPA because they are unnecessary to prevent illegal payments.

Section 102 requires all public companies to maintain an accurate accounting of the transactions and dispositions of their assets. It also requires these companies to maintain a system of internal accounting controls to ensure management awareness of, and hence accountability for, illegal payments.

The result of the GAO investigation of the impact of the FCPA on American business, published in March, 1981, is especially instructive on the impact of these accounting provisions. This report indicates how expensive it is for a company to comply with the Act's accounting provisions. Almost a quarter of the corporate respondents indicated accounting and auditing cost increases exceeding 35 percent, while over one-half estimated that compliance had increased cost by 11 to 35 percent.

Significantly, the accounting provisions affect public companies regardless of whether they engage in international business. Compliance with these provisions is particularly difficult since their interpretation is unclear.

The removal of the accounting requirements will permit less burdensome accounting practices by U.S. business, while continuing to allow the goals of the FCPA to be achieved.

The presence of criminal sanctions for bribery of foreign officials gives business management sufficient incentive to maintain proper recordkeeping and control even without section 102. Pervasive Federal rules on accounting practices have not been necessary for the enforcement of domestic bribery laws or other criminal laws prohibiting misuse of corporate assets. There appears no justification for such rules with regard to foreign bribery.

CONFUSION OVER PERMISSIBLE PAYMENTS

Certain facilitating payments are permissible under the Act if made to foreign officials whose duties "are essentially ministerial or clerical."

In practice, this term has sometimes proven difficult to interpret, and business opportunities have been lost as a result.

In Indonesia, for example, one corporation did not bid on a government contract because of uncertainty over whether facilitating payments commonly given in that country to local sales representatives and administrative personnel would violate the Act.

More attention needs to be given by the Congress to defining what types of payments are permissible. In our judgment, S. 708 is a useful starting point for that analysis in that it attempts to enumerate specific categories of exempted payments.

By having such specific exemptions the business community can be more certain that certain types of payment will not subject them to liability and thereby be more willing to export overseas.

CONCLUSION

Mr. Chairman, I appreciate the opportunity to express my views today, and I would welcome the chance to work with the Committee in the future on constructive revisions to the FCPA. I would be happy to answer any questions the Committee has.

STATEMENT OF ERNEST B. JOHNSTON, JR.

Mr. JOHNSTON. I am Ernest Johnston, Deputy Assistant Secretary for Economic and Business Affairs in the Department of State.

Mr. Chairman, I was going to give a summary but it seems to me that time is growing short so I will just submit my statement for the record.

I would like to say one thing. You brought up that cable that we sent from the State Department. I asked that that cable be sent out, and the reason I asked that that cable be sent out was exactly the reason that you are talking about right here. We went through a series of hearings in the Senate, and the Senators said, give us some examples.

Now, you asked, why did the State Department take a position, and then tell the posts what the position was, so they could find examples. I would like to tell you about that. The reason was that we had previously received a great number of indications from our posts abroad that this act was causing troubles with regard to American exports. I am not talking about the effort by the United States to prevent bribery. I think it has been made clear enough this morning that everybody involved in this business is not trying to encourage bribery.

The question is, how can this law be cleaned up in such a way that the ambiguities will not be standing in the way of our exports?

We had received sufficient information from the reports that we had previously gotten from embassies and from, the reports of conversations that we had had with businessmen. Our department came to the conclusion that the act should be improved.

After we had gone through the Senate hearings we then went to the posts. We thought it was useful to let them know what the administration position is. They don't always know exactly what is going on here in Washington. We then asked them for the examples.

[Testimony resumes on p. 305.]

[Mr. Johnston's prepared statement and attachment follow:]

TESTIMONY OF
ERNEST B. JOHNSTON, JR.
DEPARTMENT OF STATE
BEFORE THE
SUBCOMMITTEE ON TELECOMMUNICATIONS,
CONSUMER PROTECTION AND FINANCE
HOUSE COMMITTEE ON ENERGY AND COMMERCE
WEDNESDAY, DECEMBER 16, 1981

MR. CHAIRMAN AND SUBCOMMITTEE MEMBERS, I AM PLEASED TO HAVE THE OPPORTUNITY TO COMMENT ON THE FOREIGN CORRUPT PRACTICES ACT OF 1977 IN THESE OVERSIGHT HEARINGS. THE DEPARTMENT OF STATE BELIEVES THAT THE ACT HAS DETERRED THE BRIBERY OF FOREIGN OFFICIALS BY U.S. FIRMS, BUT AT SOME COSTS WHICH COULD BE AVOIDED -- PRIMARILY TO U.S. EXPORTS, BUT ALSO TO OUR FOREIGN RELATIONS.

WE FULLY SUPPORT THE GOALS OF THE FCPA. BRIBERY BY AMERICAN CITIZENS AND COMPANIES WORKS AGAINST THE INTERESTS OF THE UNITED STATES. IT HARMS THE GOOD NAME OF THIS COUNTRY, AND IT IS CONTRARY TO THE PRINCIPLES WHICH OUR PEOPLE HOLD DEAR. THOUGH CORRUPTION MAY BE MORE PREVALENT IN SOME COUNTRIES THAN OUR OWN, AMERICANS DO NOT WISH TO HAVE OUR CITIZENS ASSOCIATED WITH IT.

BRIBERY OF FOREIGN OFFICIALS IS NOT IN THE LONG-RUN INTEREST OF OUR COMPANIES. IT DOES NOT ADD TO THE NUMBER OF GOODS BEING PRODUCED AND DOES NOT INCREASE THE GOODS BEING CONSUMED. IT IS A COST WHICH EITHER MUST BE SHAVED OFF PROFITS, PASSED ON TO THE CONSUMING PUBLIC, OR SHARED -- FOR THE ENRICHMENT OF PARTICULAR INDIVIDUALS AT THE COST OF SOCIETY.

ILLICIT PAYMENTS TO FOREIGN OFFICIALS AND THE DISCLOSURE THEREOF CAN HAVE IMPORTANT RAMIFICATIONS FOR OUR FOREIGN RELATIONS, NATIONAL SECURITY, AND ECONOMIC INTERESTS. THEY CAN WEAKEN POLITICAL STABILITY, ERODE POPULAR SUPPORT FOR FOREIGN GOVERNMENTS, AND JEOPARDIZE THE IMPORTANT INTERESTS WE SHARE WITH OUR FRIENDS ABROAD.

I DON'T NEED TO REMIND THIS SUBCOMMITTEE OF THE SERIOUS INCIDENTS WHICH PAVED THE WAY FOR THE ENACTMENT OF THE FCPA. THE ACT AND U.S. FIRMS' COMPLIANCE WITH ITS PROVISIONS HAVE REDUCED THE POSSIBILITY OF THE RECURRENCE OF SIMILAR PROBLEMS. MOREOVER, SOME REPORTS FROM OUR FOREIGN SERVICE POSTS INDICATE THE FCPA HAS GIVEN U.S. FIRMS A GOOD REASON FOR REFUSING REQUESTS FOR ILLICIT PAYMENTS.

HOWEVER, THE 1977 ACT HAS HAD UNDESIRABLE SIDE-EFFECTS BECAUSE OF ITS AMBIGUITIES AND OMISSIONS. FIRST, IT HAS UNNECESSARILY IMPEDED U.S. EXPORTS. SECOND, COMPLIANCE EFFORTS BY U.S. FIRMS HAVE IRRITATED AND EMBARRASSED SOME FOREIGN OFFICIALS. AND FINALLY, EXTENDING U.S. ANTIBRIBERY CONCEPTS EXTRATERRITORIALLY, TO SOCIETIES WITH WIDELY VARYING LAWS AND CUSTOMS, TENDS TO RAISE ISSUES WHICH ARE DIFFICULT TO RECONCILE.

I WOULD LIKE TO MAKE CLEAR THAT THESE UNDESIRABLE CONSEQUENCES CAN BE MINIMIZED -- THAT WE CAN HAVE A STRONG LAW AGAINST BRIBERY WITHOUT CAUSING THESE HARMFUL SIDE-EFFECTS.

IN REGARD TO MY FIRST POINT, REPORTS FROM OUR FOREIGN SERVICE POSTS INDICATE THAT THE ACT CREATES SERIOUS PROBLEMS FOR U.S. COMPANIES -- PROBLEMS NOT DIRECTLY ASSOCIATED WITH ITS BAN ON BRIBERY. THIS PAST SUMMER THE DEPARTMENT SURVEYED MORE THAN 115 POSTS AND FOUND THAT THE FCPA ADVERSELY AFFECTS LEGITIMATE BUSINESS TRANSACTIONS IN A NUMBER OF WAYS INCLUDING:

- PROBLEMS RELATED TO OBTAINING AND DEALING WITH LOCAL AGENTS.
- DIFFICULTIES ASSOCIATED WITH NEGOTIATING CONTRACTS FOR JOINT VENTURES.
- INCREASED OPERATING COSTS FOR ACCOUNTING AND REPORTING REQUIREMENTS.
- THE LACK OF FLEXIBILITY TO PROVIDE LEGITIMATE GIFTS.
- OVERCAUTIOUSNESS BY AMERICAN FIRMS IN ATTEMPTING TO COMPLY WITH THE ACT.

THE LATTER APPEARS TO CONFIRM FREQUENTLY HEARD COMPLAINTS BY BUSINESS THAT THE FCPA IS AMBIGUOUS AND DIFFICULT TO UNDERSTAND. AS A RESULT OF THESE DIFFICULTIES, U.S. FIRMS HAVE IN MANY INSTANCES FOREGONE LEGITIMATE EXPORTS, AVOIDED MARKETS, AND EVEN OPTED TO PLAY SUBORDINATE CONTRACTING ROLES TO FOREIGN PRIME CONTRACTORS.

WE ALSO FOUND THAT THE ACT'S IMPACT ON U.S. FIRMS OCCURS PRIMARILY IN DEVELOPING COUNTRIES WITH WHOM THE UNITED STATES TRADES SIGNIFICANTLY, PARTICULARLY IN THE MIDDLE EAST AND ASIA. I CANNOT OVERSTATE THE IMPORTANCE TO THE UNITED STATES OF SUSTAINING EXPORTS TO THESE TWO REGIONS. OF THE POSTS REPORTING FROM MIDDLE EASTERN AND ASIAN COUNTRIES WITH WHOM WE HAVE SIGNIFICANT COMMERCIAL RELATIONS, APPROXIMATELY SIXTY PERCENT INDICATED THAT THE FCPA HAS CAUSED A LOSS OF COMPETITIVENESS FOR U.S. FIRMS FROM PROBLEMS NOT DIRECTLY ASSOCIATED WITH ITS PROHIBITION OF BRIBERY.

THE 1981 SURVEY FINDINGS ARE CONSISTENT WITH PREVIOUS FOREIGN SERVICE REPORTING AND WITH THE CONCLUSIONS REACHED BY SENATOR BENTSEN'S EAST ASIA STUDY MISSION, A VENTURE SUPPORTED BY THE DEPARTMENT OF STATE. I HAVE ATTACHED A COPY OF THE SURVEY REPORT TO MY WRITTEN REMARKS AND WOULD APPRECIATE IT BEING INCLUDED IN THE HEARING RECORD.

CONGRESS ENVISAGED THAT SOME EXPORTS WOULD BE LOST AS A CONSEQUENCE OF THE FCPA. HOWEVER THE LOSS OF COMPETITIVENESS AND LEGITIMATE EXPORTS, DUE TO A LAW WITH SOME AMBIGUOUS AND OVERLY HARSH PROVISIONS WHICH DOES NOT FULLY TAKE INTO ACCOUNT SITUATIONS THAT LAW-ABIDING U.S. FIRMS COMMONLY FACE ABROAD, CANNOT IN GOOD CONSCIENCE BE PERMITTED.

THE SECOND SIDE-EFFECT -- IRRITATION AND EMBARRASSMENT OF FOREIGN OFFICIALS AND OTHER PROMINENT FOREIGN CITIZENS CAUSED BY U.S. FIRMS' ATTEMPTS TO COMPLY WITH THE ACT -- IS OF PARTICULAR CONCERN TO THE DEPARTMENT OF STATE.

AMERICAN FIRMS OPERATING ABROAD OFTEN ARE REQUIRED BY LAW OR CUSTOM, OR FOR REASONS OF EFFECTIVENESS, TO BE REPRESENTED BY LOCAL AGENCIES. IN MANY INSTANCES FOREIGN OFFICIALS CONTROL, OR ARE ASSOCIATED WITH, AGENCIES WITH WHICH U.S. COMPANIES MUST DO BUSINESS. UNFORTUNATELY, THE FCPA IN A NUMBER OF INSTANCES HAS CAUSED AMERICAN FIRMS TO AVOID DEALING WITH SUCH AGENCIES.

BESIDES PLACING THE FIRMS AT A COMPETITIVE DISADVANTAGE, THIS HAS IRRITATED AND EMBARRASSED SOME FOREIGN OFFICIALS. THEY RESENT THE FCPA AND WHAT THEY PERCEIVE AS ITS GENERAL INFERENCE OF MISCONDUCT ON THEIR PART.

U.S. BUSINESSMEN IN THE UNITED ARAB EMIRATES FACE A SITUATION IN WHICH IT IS COMMON FOR AN INDIVIDUAL TO WORK IN A GOVERNMENTAL CAPACITY IN THE MORNING AND IN A COMMERCIAL POSITION IN THE AFTERNOON. HOWEVER, OUR EMBASSY IN THAT COUNTRY HAS REPORTED THAT IT IS MOST UNUSUAL FOR SUCH AN OFFICIAL TO USE HIS OFFICE FOR SELF-GAIN. THE EMBASSY ALSO REPORTED THAT MANY REPUTABLE U.A.E. BUSINESSMEN RESENT WHAT THEY PERCEIVE AS A QUESTIONING OF THEIR OWN HONESTY IN BUSINESS DEALINGS WITH U.S. FIRMS INTENT ON COMPLYING WITH THE FCPA.

THE U.S. EMBASSY IN MUSCAT REPORTED THAT OMANI NATIONALS ARE SENSITIVE TO THE FACT THAT HOLDING GOVERNMENT OFFICE AND PURSUING OUTSIDE BUSINESS INTERESTS AT THE SAME TIME OFTEN CREATE AT LEAST A PRIMA FACIE APPEARANCE OF POTENTIAL FCPA PROBLEMS.

SOME FOREIGN OFFICIALS ALSO HAVE BEEN IRRITATED OR EMBARRASSED WHEN U.S. COMPANIES, IN COMPLYING WITH THE FCPA, HAVE BEEN RELUCTANT TO ALLOW THEM TO PARTICIPATE IN JOINT VENTURES AND STOCK OWNERSHIP. AGAIN, THEY RESENT THE INFERENCE OF MISCONDUCT ON THEIR PART.

IN 1981 OUR EMBASSY IN SAUDI ARABIA DESCRIBED DIFFICULTIES WHICH THE FCPA CAUSES FOR U.S. FIRMS WHICH ARE ATTEMPTING TO ENTER INTO JOINT VENTURE AGREEMENTS WITH SAUDI FIRMS. BESIDES DESCRIBING TWO CASES IN DETAIL, WHICH ARE CITED IN THE ATTACHED SURVEY REPORT, THE EMBASSY REPORTED THAT IN ORDER TO PROTECT THEMSELVES FROM THE UNCERTAINTIES OF THE FCPA, AMERICAN COMPANIES SOMETIMES INSIST THAT PROTECTIVE LANGUAGE BE INSERTED IN CONTRACTS. THE SAUDIS GENERALLY TAKE OFFENSE AT THE IMPLICATION THAT THEY ARE CORRUPT, BAD FEELINGS OCCUR, NEGOTIATIONS ARE EXTENDED AT CONSIDERABLE COST, AND AGREEMENTS SOMETIMES ARE JEOPARDIZED.

THE DEPARTMENT FEELS THAT ANY AMENDMENT OF THE FCPA SHOULD MAKE CLEAR THAT INVOLVEMENT OF FOREIGN OFFICIALS IN LEGITIMATE BUSINESS TRANSACTIONS PER SE IS NOT A VIOLATION OF THE LAW. U.S. FIRMS NEED AND DESERVE ASSURANCE THAT CONDUCTING LEGITIMATE TRANSACTIONS WITH AGENCIES WHICH ARE ASSOCIATED WITH FOREIGN OFFICIALS, AND ALLOWING SUCH OFFICIALS TO PARTICIPATE IN JOINT VENTURES OR STOCK OWNERSHIP, ARE PERMITTED. HOWEVER, IT SHOULD ALSO BE CLEAR THAT OFFERING SUCH AN INDIVIDUAL A BRIBE TO USE HIS INFLUENCE TO OBTAIN A CONTRACT FOR THE U.S. FIRM IS ILLEGAL. THIS KIND OF CHANGE COULD BE ADDRESSED IN SEVERAL WAYS -- IN AN AMENDMENT, IN THE LEGISLATIVE HISTORY OR IN DEPARTMENT OF JUSTICE GUIDELINES TO BUSINESS.

THE LAST POINT -- REGARDING THE DIFFICULTIES PRESENTED BY THE EXTRATERRITORIAL REACH OF THE ACT -- IS ALSO OF PARTICULAR CONCERN TO THE DEPARTMENT OF STATE. THESE DIFFICULTIES RAISE BOTH THEORETICAL QUESTIONS AND PRACTICAL PROBLEMS.

THE THEORETICAL QUESTIONS PRESENT LEGAL ISSUES RELATING TO THE APPROPRIATE EXTRATERRITORIAL REACH OF ONE COUNTRY'S CRIMINAL JURISDICTION. THE PROBLEMS ARISE WHEN THE LAW IS APPLIED THROUGH COMPLIANCE EFFORTS OF U.S. FIRMS AND IF INFORMATION REGARDING ACTIVITIES OF FOREIGN OFFICIALS IS MADE PUBLIC.

IN MAY THE UNITED KINGDOM EXPRESSED CONCERN TO OUR EMBASSY IN LONDON THAT PROVISIONS OF THE FCPA COULD BE APPLIED "TO PERSONS INCORPORATED AND/OR CARRYING ON BUSINESS

IN" THAT COUNTRY. TO BE SURE, THE UNITED KINGDOM DOES NOT CONDONE ILLICIT PAYMENTS. HOWEVER, THE GOVERNMENT OF THAT COUNTRY BELIEVES, AS A MATTER OF ITS OWN SOVEREIGN JURISDICTION, THAT COMPANIES INCORPORATED AND DOING BUSINESS IN THE UNITED KINGDOM, WHATEVER THEIR OWNERSHIP, ARE SUBJECT ONLY TO U.K. LAW IN RESPECT TO THEIR ACTIVITIES IN THE UNITED KINGDOM. THE U.K. EXPRESSED THAT VIEW FORMALLY IN DIPLOMATIC NOTE NO. 146 OF JULY 23, 1981. A COPY OF THE NOTE IS INCLUDED IN OUR RECENT REPLY TO CONGRESSMAN WIRTH'S LETTER OF OCTOBER 5.

THE FCPA RECENTLY WAS CITED AS A FACTOR IN THE DECISION BY THE BRITISH GOVERNMENT TO DISALLOW THE ACQUISITION OF THE DAVY CORPORATION, A BRITISH FIRM, BY THE ENSERCH CORPORATION, AN AMERICAN COMPANY. IN THAT CASE THE U.K. MONOPOLIES AND MERGER COMMISSION FELT THAT IF ACQUIRED BY ENSERCH, THE FCPA MIGHT NEGATIVELY AFFECT DAVY'S BUSINESS PROSPECTS IN CERTAIN COUNTRIES. THE COMMISSION STATED THAT THIS COULD OCCUR BECAUSE ENSERCH'S POLICY, IN COMPLYING WITH THE FCPA, IS "TO AVOID ALTOGETHER THE USE OF ANY AGENT WHO IS A GOVERNMENT EMPLOYEE IN A POSITION RELEVANT TO THE CONTRACT EVEN IF THE COMMISSION IS REASONABLE AND THE INDIVIDUAL EFFECTIVE AND HONEST."

THE U.K. HAS EXPRESSED CONCERN ALSO ABOUT THE EXTRATERRITORIAL REACH OF OTHER U.S. LAWS INCLUDING ANTITRUST AND ANTIBOYCOTT STATUTES, THE EXPORT ADMINISTRATION ACT, THE INTERNATIONAL EMERGENCY ECONOMIC POWERS ACT, AND THE PRECURSOR,

THE TRADING WITH THE ENEMY ACT. DISCUSSIONS OF THEIR CONCERNS ABOUT THESE LAWS, AND SPECIFICALLY ABOUT THE FCPA, TOOK PLACE IN WASHINGTON IN OCTOBER, 1981, AND WILL CONTINUE AT A LATER DATE.

IN GENERAL, THE DEPARTMENT HAS OBSERVED THAT A NUMBER OF COUNTRIES ARE FINDING THE EXTRATERRITORIAL SCOPE OF U.S. LEGISLATION MORE OBJECTIONABLE THAN THEY DID IN THE PAST. OTHER COUNTRIES, SUCH AS AUSTRALIA, CANADA AND WEST GERMANY, ALSO HAVE EXPRESSED CONCERN ABOUT THE REACH OF VARIOUS U.S. LAWS. THIS OBSERVATION IS ALSO REFLECTED IN AN AUGUST 31, 1981 SPEECH IN WHICH THE ATTORNEY GENERAL NOTED THAT "THERE IS A GROWING WAVE OF SENTIMENT SUGGESTING THAT THE UNITED STATES HAS ADOPTED MUCH TOO BROAD A VIEW OF ITS JURISDICTION OVER ACTIVITIES THAT AFFECT MORE THAN ONE NATION AND INVOLVE CONDUCT NOT WHOLLY CONFINED TO OUR TERRITORY."

ANOTHER EXAMPLE OF DIFFICULTIES WHICH CAN OCCUR DUE TO THE EXTRATERRITORIAL NATURE OF THE FCPA WAS REPORTED THIS YEAR BY OUR EMBASSY IN BERN. IT REPORTED THAT THE LEGAL AFFAIRS COMMITTEE OF THE SWISS-AMERICAN CHAMBER OF COMMERCE, A PRIVATE GROUP, STUDIED FCPA-ASSOCIATED REQUIREMENTS THAT U.S. FIRMS PLACE ON REPRESENTATIVES IN SWITZERLAND. THE COMMITTEE CONCLUDED THAT INVOLVED AMERICAN SUPPLIERS HAD TAKEN AN EXAGGERATED VIEW OF THEIR OBLIGATIONS UNDER THE ACT AND THAT CARRYING OUT SUCH FCPA COMPLIANCE REQUIREMENTS IN

THAT COUNTRY APPEARED TO VERGE ON VIOLATION OF SWISS LAW. WHILE INTERPRETATION OF SWISS LAW RESTS WITH THE SWISS AUTHORITIES AND COURTS, THIS PRIVATE OPINION REFLECTS A LEGITIMATE CONCERN OF THE BUSINESS COMMUNITY.

THE EXTRATERRITORIAL APPLICATION OF U.S. ANTIBRIBERY LEGISLATION IN FOREIGN COUNTRIES ALSO CREATES PROBLEMS ASSOCIATED WITH POSSIBLE PUBLIC DISCLOSURES WHICH MAY OCCUR IN CONNECTION WITH ENFORCEMENT OF THE ACT. PAST PUBLIC DISCLOSURES, FROM SOME ENFORCMENT PROCEEDINGS AND PRESS LEAKS, REGARDING BOTH LEGITIMATE AND ILLICIT PAYMENTS TO FOREIGN OFFICIALS BY U.S. FIRMS, HAVE EMBARRASSED THE OFFICIALS AND CREATED DIFFICULTIES IN OUR RELATIONS WITH THEM. THIS IS ESPECIALLY TRUE IN COUNTRIES WHERE CERTAIN PRACTICES ARE LEGITIMATE UNDER THE PREVAILING LAWS AND CUSTOMS. IN SOME CASES, THE HOST COUNTRIES HAVE INVESTIGATED AND/OR PROSECUTED THE OFFICIALS INVOLVED, WHILE IN OTHERS THIS HAS NOT BEEN DONE. HOST GOVERNMENT DECISIONS REGARDING PROSECUTION OF THEIR OFFICIALS ARE BASED, INTER ALIA, ON THE LAWS AND CUSTOMS OF THE HOST COUNTRY, INTERNAL POLITICAL CONSIDERATIONS, AND PARTICULARS OF THE SPECIFIC CASE.

U.S. RELATIONS WITH FOREIGN OFFICIALS CAN BE COMPLICATED WHEN THE NAMES OF SUCH OFFICIALS ARE IMPLICATED, IN ONE WAY OR ANOTHER, IN AN FCPA ENFORCEMENT PROCEEDING. THE SITUATION CAN BE FURTHER AGGRAVATED WHEN THE FOREIGN OFFICIAL IS

EXONERATED IN HIS OWN COUNTRY. MOREOVER, FCPA-RELATED IMPLICATIONS, PROVED OR NOT, OF FOREIGN OFFICIALS CAN AFFECT THEIR ATTITUDES TOWARD THE UNITED STATES FOR AN INDEFINITE PERIOD OF TIME. THIS IS A PARTICULARLY IMPORTANT CONSIDERATION WHEN THE FOREIGN OFFICIAL IS HIGH-RANKING OR ACHIEVES HIGHER OFFICE AT A LATER DATE.

I BELIEVE THAT IT IS IMPORTANT TO TAKE THIS OPPORTUNITY TO POINT OUT THAT THE DEPARTMENTS OF STATE AND JUSTICE AND THE SEC HAVE WORKED VERY CLOSELY AND SUCCESSFULLY TO MINIMIZE FOREIGN RELATIONS PROBLEMS WHICH MAY OCCUR AS A RESULT OF THIS TYPE OF ENFORCEMENT PROCEEDINGS. EXAMPLES OF INSTANCES IN WHICH THIS COOPERATION WAS CARRIED OUT ARE INCLUDED IN THE DEPARTMENT'S REPLY TO THE PREVIOUSLY MENTIONED LETTER FROM THE SUBCOMMITTEE.

WITH REGARD TO THE PUBLIC DISCLOSURE OF LEGITIMATE TRANSACTIONS, IN 1979 AN EMBASSY IN ASIA REPORTED THAT HOST COUNTRY JOINT VENTURE PARTNERS AND BUSINESS ASSOCIATES WERE BECOMING INCREASINGLY UNEASY ABOUT THE POTENTIAL DISCLOSURE OF THEIR BUSINESS ACTIVITIES IN CONNECTION WITH FCPA ENFORCEMENT ACTIONS. LOCAL BUSINESSMEN FEAR THAT THE LOCAL PRESS AND THE OPPOSITION POLITICAL PARTIES CAN PORTRAY LEGITIMATE COMMISSIONS AS ILLICIT PAYMENTS.

IN SUMMARY, WE MUST BALANCE TWO COMPETING INTERESTS: RESTRICTING POTENTIALLY HARMFUL OVERSEAS BUSINESS PRACTICES BY U.S FIRMS WHILE KEEPING WITHIN ACCEPTABLE LIMITS THE

IMPOSITION OF OUR OWN STANDARDS ON OTHERS. I THINK ONE PARTICULAR PROVISION IN S.708 WOULD HELP ACHIEVE SUCH BALANCE BY EXCLUDING FROM PROSECUTION ACTIONS WHICH ARE LEGAL IN THE COUNTRY WHERE THEY OCCUR. IF SUCH A PROVISION WERE ENACTED, IT WOULD REDUCE SIGNIFICANTLY THE IMPRESSION THAT THE UNITED STATES IS IMPOSING ITS OWN CENSORIOUS JUDGMENTS ON STANDARDS WHICH OTHER COUNTRIES MAY CHOOSE TO SET FOR THEMSELVES.

I WOULD LIKE NOW TO COMMENT ON THE STATUS OF EFFORTS TO ACHIEVE AN INTERNATIONAL AGREEMENT ON ILLICIT PAYMENTS. THE UNITED STATES HAS VIGOROUSLY PRESSED THE NEGOTIATION OF SUCH AN AGREEMENT SINCE 1976. ALTHOUGH A U.N.ECONOMIC AND SOCIAL COUNCIL (ECOSOC) COMMITTEE COMPLETED LENGTHY PREPARATORY WORK IN 1979 ON A LARGELY AGREED-UPON DRAFT AGREEMENT ON ILLICIT PAYMENTS, THE ECOSOC AND THE U.N. GENERAL ASSEMBLY (UNGA) EACH FAILED FOR TWO YEARS IN A ROW TO TAKE ANY ACTION TO CONCLUDE AN AGREEMENT. THIS WAS LARGELY DUE TO THE INSISTENCE OF THE DEVELOPING COUNTRIES ON LINKING AN ILLICIT PAYMENTS TREATY WITH A STILL UNCOMPLETED CODE OF CONDUCT FOR TRANSNATIONAL CORPORATIONS. THE UNITED STATES AND ITS MAJOR WESTERN ALLIES CONSISTENTLY OPPOSED SUCH LINKAGE.

AT THE VENICE ECONOMIC SUMMIT IN JUNE 1980, OUR GOVERNMENT MADE A COMMITMENT TO WORK IN THE U.N. TOWARD AN ILLICIT PAYMENTS AGREEMENT BUT, IF THAT EFFORT FALTERED, TO SEEK TO CONCLUDE AN AGREEMENT AMONG THE SUMMIT COUNTRIES, OPEN TO ALL, WITH THE SAME OBJECTIVE.

AFTER THE FALL 1980 UNGA FAILED TO REACH AGREEMENT ON THE TREATY, OUR REPRESENTATIVE STATED THAT THE U.S. INTENDED TO CONSULT WITH OTHER INTERESTED STATES REGARDING ALTERNATIVE MEANS OF ACHIEVING A TREATY OUTSIDE THE U.N.

THIS ISSUE WAS NOT ADDRESSED AT THE 1981 OTTAWA SUMMIT. THE UNITED STATES SOUGHT A SUMMIT AGENDA FOCUSED ON THE MOST URGENT PROBLEMS CONFRONTING THE MAJOR INDUSTRIALIZED COUNTRIES -- SUCH AS ENERGY, EAST-WEST TRADE AND RELATIONS WITH DEVELOPING COUNTRIES -- RATHER THAN A LONG, DETAILED LIST OF AGENDA ITEMS. THERE WAS ALSO THE CONSIDERATION THAT CONGRESS HAD BEFORE IT A PENDING BILL WHICH MIGHT RESULT IN LEGISLATION STRENGTHENING OUR INTERNATIONAL NEGOTIATING POSITION.

THIS PAST OCTOBER WE DID, HOWEVER, ASK OTHER OECD COUNTRIES IF THEY WOULD BE INTERESTED IN ACHIEVING AN AGREEMENT AMONG ONLY OECD MEMBERS. WE FOUND NO POSITIVE INTEREST BY THEM IN PURSUING SUCH AN AGREEMENT AND RECEIVED SOME OBJECTIONS TO DOING SO. THE LATTER CENTERED ON THE MEMBER COUNTRIES' JURISPRUDENTIAL DIFFERENCES, WHICH MAKE ACHIEVEMENT OF SUCH AN AGREEMENT DIFFICULT.

IN THE PRESENT CIRCUMSTANCES, IT SEEMS UNLIKELY THAT EARLY PROGRESS CAN BE MADE TOWARD CONCLUSION OF AN INTERNATIONAL AGREEMENT ON ILLICIT PAYMENTS. NEVERTHELESS, THE DEPARTMENT OF STATE CONTINUES TO SUPPORT THE ACHIEVEMENT OF

SUCH AN AGREEMENT FOR TWO REASONS. FIRST, IT WOULD ENHANCE EFFORTS TO REPRESS BRIBERY AND EXTORTION IN INTERNATIONAL COMMERCIAL TRANSACTIONS. SECOND, IT WOULD REDUCE THE DISADVANTAGE TO U.S. FIRMS, WITH REGARD TO FOREIGN COMPETITORS, CAUSED BY THE ENACTMENT AND ENFORCEMENT OF THE FCPA.

I WOULD LIKE TO POINT OUT THAT ENACTMENT OF A LAW, SIMILAR TO S.708, WHICH PROHIBITS BRIBERY WITHOUT UNDUE HARM TO EXPORTS, WOULD ENHANCE OUR EFFORTS TO ACHIEVE AN INTERNATIONAL AGREEMENT. OUR TRADING PARTNERS ARE CERTAINLY AWARE OF THE PROBLEMS AMERICAN BUSINESSMEN HAVE EXPERIENCED UNDER THE CURRENT LAW.

IN CONCLUSION, I HOPE THIS SUBCOMMITTEE WILL CONSIDER AMENDMENT OF THE FCPA AT AN EARLY DATE. AMENDMENT ALONG THE LINES OF S. 708 WOULD PROVIDE A MORE REALISTIC STANDARD FOR U.S. CORPORATE ACTIVITIES OVERSEAS, WOULD ALLEVIATE THE UNNECESSARY IMPEDIMENTS TO U.S. EXPORTS, WOULD REDUCE THE IRRITANTS TO FOREIGN OFFICIALS, AND WOULD ENHANCE OUR EFFORTS TO REACH AN ACCEPTABLE INTERNATIONAL AGREEMENT. WE LOOK FORWARD TO WORKING WITH THE SUBCOMMITTEE IN FUTURE DELIBERATIONS ON THIS ISSUE.

THE FOREIGN CORRUPT PRACTICES ACT:
REPORTS FROM THE FOREIGN SERVICE

EXECUTIVE SUMMARY

This report summarizes and analyzes the responses of over 115 Foreign Service posts abroad who were asked to assess the effects of the Foreign Corrupt Practices Act of 1977 (FCPA) on U.S. exports and foreign relations. Many posts reported that the FCPA has (a) placed numerous U.S. firms at a serious competitive disadvantage in relation to foreign firms which are not restrained by similar legislation and (b) complicated the conduct of some legitimate business transactions by U.S. firms with foreign entities. These results occur primarily in developing countries with which the United States trades significantly, particularly in the Middle East and Asia.

Although the Act's prohibition on bribery is partially responsible, several factors associated with American firms' complying with the FCPA also contribute to these problems. These include problems related to obtaining and dealing with agents, contracting problems, increased operating costs for accounting and reporting requirements, the lack of flexibility to provide legitimate gifts, and overcautiousness in attempting to comply with the Act. The latter appears to confirm frequently heard complaints by business that the Act is ambiguous and difficult to understand.

As a result of these difficulties, U.S. firms have:

- foregone some apparently legitimate exports,
- avoided some markets, and
- opted to play subordinate contracting roles to foreign prime contractors.

Many posts described ways in which the FCPA has adversely affected the ability of U.S. businesses to compete, but only a few provided concrete examples of business opportunities which American firms lost due to the Act. This does not necessarily mean that exports have not been foregone. Numerous posts indicated that by nature such information is difficult to obtain and is not something businessmen would normally tell embassy officers. Firms are reluctant to discuss such matters since providing detailed information for public use could damage prospects for future business.

Very few posts reported FCPA-associated foreign relations strains. However, several reports described situations in which efforts by U.S. firms to comply with the FCPA, with inherent inferences of impropriety, irritated foreign officials and prominent citizens of foreign countries.

FINDINGS

Foreign Service posts were requested in May 1981 to report on the effects of the FCPA. In particular, information regarding foregone exports, loss of competitiveness and past or potential foreign relations problems was sought. More than 115 posts provided relevant information. Their reports reflect the views both of embassy officers and of U.S. businesses operating abroad, to the degree they have discussed their problems with embassy officers.

TRENDS

The reports indicate that many U.S. business persons abroad do not understand the Act or how it is enforced, and experience difficulties in complying with it, aside from the prohibition against bribery, which disadvantage them competitively. This occurs primarily in developing countries with which the United States trades significantly, especially in countries where facilitating, "grease" payments are commonly associated with business transactions and where government officials have major interests in private business. Conversely, U.S. firms in developed countries experience very few difficulties of this nature, except where their operations in third countries are affected.

As was anticipated, posts in countries with which we conduct little business, such as Rwanda and Cyprus, reported that the FCPA generally is not a significant deterrent to exporting. Over forty reports were received from such countries.

Thirty-nine percent of the posts in countries with which the United States has significant commercial relations reported that the Act has caused a loss of competitiveness for U.S. firms from problems not directly associated with its prohibition of bribery. By geographic regions the percentages are:

Middle East and South Asia	59%
East Asia	60%
Africa	50%
South and Central America, and the Caribbean	41%
Europe	15%

The reports reflect that in order to avoid FCPA-related problems, U.S. firms sometimes are overzealous in their efforts to comply. This leads them to forego legitimate exports, to avoid doing business in certain countries and to remove themselves from competition on principal contracts, accepting instead roles as subcontractors, with other foreign firms entering into the contractual relationship with the foreign government concerned.

LOSS OF COMPETITIVENESS

The loss of competitiveness cited in reports is attributed to several causes, as defined below.

Problems Associated with Agents

Several reports described problems regarding agents which are related to FCPA-compliance efforts of U.S. firms. Our embassy in Oman reported that because it is so common for prominent Omani businessmen to also hold government office, the FCPA causes special problems. Among major Omani firms only a handful have no government officials among their principals. U.S. companies seeking local representation, as required by Omani law, often find that the few Omani firms not owned by government officials already represent non-U.S. competitors. U.S. firms are thus faced with a difficult choice: if they select an Omani firm which does not include government officials among its owners, but which represents a business competitor, marketing is bound to suffer. On the other hand, if they select a firm which does not represent competitors, but which has government officials as owners, problems of compliance with the FCPA may arise. The embassies in Qatar and the United Arab Emirates reported similar problems.

Madrid reported that, according to the manager of an American firm in Spain, due to the FCPA some U.S. firms no longer compensate agents by commission, but rather employ "representatives" who work for a fixed fee regardless whether a sale requires six months or six years of effort. In the case of his own firm, the manager had not been authorized to grant a bonus to a salesman in Latin America who was responsible for concluding a large sale, and who was about to land another big contract. This naturally discourages initiative and hard work by employees.

In Liberia it has long been the predominant practice for foreign firms to take on Liberian partners or agents whose contributions to a joint venture are their array of contacts and their ability to work out problems with local officials. Representatives of several U.S. firms there told Embassy officials that fear of liability under the FCPA for the unsanctioned actions of local partners or agents has led to reliance on more expensive expatriates, in lieu of Liberian entrepreneurs. This naturally has made the U.S. firms less competitive.

Contracting Problems

The embassy in Saudi Arabia cited two examples of contracting problems. The first concerned efforts of an American firm to enter into a joint venture agreement with a Saudi firm. Both the American and the Saudi firms were large and reputable. While negotiations were underway, the partners-to-be actively pursued a large Saudi government contract and received assurances they would get the award. To protect itself from perceived unknowns of the FCPA, the U.S. firm insisted on protective language in the contract. The Saudi firm took umbrage at the implication that it and its officers were corrupt and dealing in illicit practices. Negotiations were extended at considerable cost. In the meantime, the Government of Saudi Arabia, unwilling to wait any longer, awarded the contract to a third country firm. The joint venture may never be worked out because of bad feelings which were generated in the contract negotiations and due to the loss of the contract.

The second case pertained to negotiations concerning an industrial joint venture involving more than \$100 million. Because of the large amount of money involved and the fact that there is virtually no market in Saudi Arabia for shares, the American company insisted on a buy-out provision in the contract. As extra protection against problems with the FCPA, the American firm's lawyer tied the buy-out clause to the Act by inserting a provision saying that if the Saudis acted contrary to provisions of the FCPA, the buy-out clause would be triggered and the American firm could demand to be released from the joint venture. Negotiations had been going well and the lawyers felt agreement was imminent. However, when all other details had been worked out, one of the Saudis involved brought up the problem of the buy-out clause. His feeling was that the FCPA language inserted in the contract was offensive, but could be accepted since not to do so would preclude doing business with the American firm. The question of tying the buy-out clause to the FCPA, however, was too much. Perceiving the law as vague, the Saudi side felt it would be open to the possibility that the U.S. firm could pull out and demand compensation at any time by claiming that the law had been broken. The two sides were unable to overcome the problem posed by the tying clause and, although negotiations continued for some months, the joint venture never materialized.

Increased Costs

A number of posts reported that the FCPA has reduced the competitiveness of U.S. firms due to increased costs to meet accounting and reporting requirements. The embassy in Caracas indicated that the most important impact of the Act on U.S. business in Venezuela is the additional costs it has imposed on firms in the form of more cumbersome accounting procedures. The embassy reported that estimates of increases in accounting costs run as high as 30 percent and that such increased costs clearly reduce the ability of U.S. companies to compete for contracts.

Malaysia reported that the main complaint regarding the FCPA is that companies, even with respect to activities legal in both Malaysia and the United States, find the reporting requirements excessively onerous. One American company manufacturing in Malaysia informed the embassy that the records they are required to keep in conjunction with legitimate customs duty drawbacks cost them tens of thousands of dollars a year.

Overcautious Compliance by U.S. Firms

A number of posts indicated that U.S. firms exercise great caution to ensure compliance with the Act. Since many companies consider the Act ambiguous, overzealous compliance efforts sometimes cause serious problems and increase operating costs. The embassy in Quito reported that some Ecuadorean branches of U.S. companies and banks require their professional-level employees to sign statements acknowledging they are aware of the provisions of the FCPA and will do nothing to violate it. Several local company representatives informed our embassy in Cairo that lawyers at their corporate headquarters tend to interpret the Act very strictly and that where it is ambiguous, their legal staffs rule on the side of caution.

American businessmen in Malawi indicated to our embassy that, in other nearby African countries, they have lost sales to foreign competition because of their overcautiousness in dealings with their agents. They attributed this to the FCPA being unclear about what practices are prohibited. U.S. business representatives in Chile complain of additional costs of doing business because of ambiguities of the Act. They maintain that to be clearly pure under the law, corporate controls and reporting requirements far exceed actual stipulations of the FCPA.

Gifts

Some posts indicated that the inability to provide gifts, which could in no way be construed as bribes, has hindered U.S. export efforts. Baghdad reported that the primary impact of the FCPA in Iraq has been to prevent U.S. firms from offering free air transportation to the U.S. for plant inspection by and sales briefings to prospective Iraqi buyers who often want a first hand look at a company's capabilities. European and Japanese firms provide such trips. Another embassy reported in detail that efforts of a U.S. firm to put together a cooperative arrangement with a foreign firm have been seriously hampered because their legal staff, in complying with the FCPA, will not allow the U.S. firm to fund a visit for representatives of the foreign company to examine the U.S. firm's plant and facilities. The negative impact of this action is greater because the foreign firm previously funded a trip for representatives of the U.S. firm to examine their facilities.

Our embassy in Athens was informed by the Middle East director of a prominent American management consulting firm that his company, under the current provisions of the FCPA, will no longer permit him to extend a visiting, non-clerical, senior Arab government technocrat a car and driver to meet him at the airport, or a basket of fruit for his hotel room, despite the fact that such amenities are not considered unusual or improper in that part of the world.

LOST OR FOREGONE SALES

Although many posts described ways in which the FCPA has adversely affected the ability of U.S. businesses to compete, only a few provided concrete examples of business opportunities which American firms lost due to the Act. This should not be taken as evidence that sales have not been lost. Many posts reported that by nature, such information is difficult to develop and document. Companies are reluctant to discuss such matters since providing detailed information for public use could damage prospects for future business. Several embassies reported sales which were believed lost because of bribes offered by foreign competitors. One embassy reported that following consultations with U.S. federal authorities, an American corporation believed it should not sign an agency agreement with a particular foreign firm since it is controlled by a senior official of the foreign government. On learning of this, the foreign government official threatened to ban the U.S. firm from doing business in that country. Potentially, this case had obvious implications for official relations.

The embassy in Oman reported that a large U.S. firm has encountered difficulty over the past couple of years in its efforts to obtain a local representative. After a series of discussions, the firm ultimately narrowed the field to one Omani firm which it felt could best represent its interests. However, the U.S. firm has been unable to conclude an agreement due to potential problems arising under the FCPA. As the firm's business runs in multimillion dollar contracts involving proprietary technology, lost U.S. exports may have been substantial.

Our embassy in Bonn reported that, according to a U.S. Chamber of Commerce official, in order to avoid FCPA problems U.S. firms bidding in third countries often have to accept a role as subcontractors while German firms serve as prime contractors. The embassy in Brussels cited the following example of this, but added that the company involved is not willing to document it. The post reported that a U.S. construction firm was interested in bidding on a project in a Middle Eastern country, but was convinced that nothing could be done in that country without the payment of commissions and "grease" payments. It therefore decided that it did not want to be the prime contractor and modified its strategy so that it would be a subcontractor for a European prime contractor, thereby accepting a smaller portion of the project.

The Embassy in Saudi Arabia reported that the FCPA intimidates some medium-sized firms from attempting to conduct business at all in that country. The firms are unwilling to expose themselves to such confused regulations without extensive legal advice that is beyond their means. Another embassy reported that an individual seeking to represent an American manufacturer abroad was informed by the company that it had given up exporting because it did not wish to run afoul of the FCPA.

FOREIGN RELATIONS PROBLEMS

The Act does not appear to have created serious bilateral strains. However, several posts provided information which indicates a serious potential for such problems.

Some posts reported that officials of foreign governments and other prominent foreign citizens have been irritated or embarrassed because U.S. firms were reluctant to allow their participation in projects, because of FCPA enforcement actions, and because of inferences of impropriety associated with compliance efforts of U.S. firms. The embassy in the United Arab Emirates reported that the U.S. image in that country

suffers because many reputable businessmen in the UAE resent what they perceive as a questioning of their own honesty in business dealings with U.S. firms intent on complying with the FCPA. The embassy in Oman reported that Omanis are sensitive to the fact that holding government office and pursuing outside business interests at the same time often create at least a prima facie inference of potential FCPA problems.

Our embassy in Saudi Arabia reported that in order to protect themselves from the uncertainties of the FCPA, American firms sometimes insist that protective language is inserted in contracts. The Saudis generally take offense at the implication that they are corrupt, bad feelings occur, negotiations are extended at considerable cost and agreements are jeopardized.

The United Kingdom has expressed concern about the FCPA's extraterritorial reach, a concern which extends to U.S. antitrust, antiboycott and other legislation as well. The extraterritorial reach of U.S. antitrust law also has been of serious concern to several other countries.

The Legal Affairs Committee of the Swiss-American Chamber of Commerce, a private group, studied FCPA-associated requirements that U.S. firms place on representatives in Switzerland. It concluded that involved American suppliers had taken an exaggerated view of their obligations and that carrying out such FCPA compliance practices in that country appeared to verge on violation of Swiss law. While interpretation of Swiss law rests with the Swiss authorities and courts, this private opinion reflects a legitimate concern of the business community.

CONCLUSION

Information available from Foreign Service posts strongly indicates that the FCPA undermines the competitiveness of U.S. firms abroad in ways not directly associated with the Act's prohibition against bribery. This is particularly evident in underdeveloped countries with whom the U.S. has significant commercial relations. Overzealous compliance efforts of U.S. businesses, apparently rooted in a lack of understanding of the FCPA, adversely affect business transactions and sometimes irritate citizens of the host country. Previous reports from Foreign Service posts provided similar information. The latest reports indicate that these problems continue to hinder U.S. export efforts.

Mr. WIRTH. Thank you very much, Mr. Johnston.

Mr. UNGER. I might volunteer, Mr. Chairman, that I would suggest to my good friend Mr. Johnston that maybe he should send a cable asking if there are any positive aspects to the FCPA that any of these posts would like to report on.

Mr. WIRTH. I think that might be a very helpful thing to do.

Mr. JOHNSTON. Mr. Chairman, this would be a massive enterprise. I am perfectly willing to do it, but I would hate to do it—

Mr. WIRTH. We have judged the statute in one fashion. Why isn't it judged in the other?

Mr. JOHNSTON. I would be happy to do it.

Mr. WIRTH. Keeping in mind budget restraints, sending out cables from the State Department may not be a good use of taxpayers' money. If you use it on one front, however—

Mr. JOHNSTON. I would hate to get involved in a massive effort which could delay anything that the committee might be doing, but if it is helpful we would certainly be willing to send out and ask for such examples.

Mr. WIRTH. In your submission you discuss the problem of American businesses and their uncertainty in dealing with foreign agents. We have been told that this is in large part due, as you were discussing, Mr. Unger, to the "reason-to-know" standard in the Foreign Corrupt Practices Act. Yet in a number of cases brought before the passage of the act, agents were used either to accumulate funds to make bribes, or to make the actual payment of a bribe. Furthermore, it was revealed during hearings the subcommittee held earlier this fall, that these practices haven't really stopped.

In the Justice Department's recent submission to us, they told us that of the 32 current cases they are investigating under the act, where they could determine the means used to make alleged foreign bribes, 19 involved making payments through agents.

If in fact we don't want to revisit the original decision by Congress to prohibit overseas bribery, and everybody has disclaimed that as an intent, how would you suggest that we deal with the problem of a corporation's responsibility for the activities of its agent?

Mr. UNGER. One thing I would do would be to eliminate the accounting requirement. I don't think that adds anything to the responsibility for its agent, and does create a burden, a substantial burden on all U.S. business, whether they are in export or not, while at the same time not imposing the same burden on private corporations. It seems to me that it is a selective enforcement procedure.

Mr. WIRTH. If you eliminate the accounting provision, how do you possibly find out about illicit payments?

Mr. UNGER. You could make it criminal not to record any payment. We are against bribery. We certainly don't have accounting provisions in the bribery laws in the United States. There are no accounting provisions that are required to determine bribery in the United States, and we are against bribery here.

The extraterritorial reach of this law is a problem, a problem internationally and a problem to those that are exposed to it. In my testimony on another subject before the Senate Judiciary Commit-

tee, I pointed out a case where a merger was prohibited in the United Kingdom because the reach of the FCPA would then apply to a British corporation, and the American corporation was not in fact allowed to acquire that company. The extraterritorial or transnational reach of a number of our laws is causing great consternation with our trading partners today. This is one problem that comes up most often in those international discussions.

I believe bribery should be outlawed. It is outlawed domestically and I would think that the same set of rules and facts should apply internationally.

Mr. WIRTH. Let me ask the question again. If you eliminate the accounting provision, how do you reach the activities of agents?

Mr. UNGER. The accounting provisions don't reach them now. They simply require any payment to be accounted for.

Mr. WIRTH. If you eliminate "reason to know" and you eliminate the accounting provisions, how do you get to the agent?

Mr. UNGER. I think we can define the burden in a more precise way than reason to know.

Mr. WIRTH. OK, the Senate bill attempts to do that. We discussed earlier the ambiguities in the Senate language with Mr. Brock. Another ambiguity is created. The Senate bill says that a company is liable only if it "directly authorizes, expressly or through a course of conduct, a corrupt payment."

What is a "course of conduct"? Is that the way of getting at it? We are not going to talk about his "reason to know," but we are going to talk about his "course of conduct." What is a "course of conduct"?

Mr. UNGER. I would think if you asked me to opt between trying to define one or the other, I would choose course of conduct every time.

Mr. WIRTH. How would you define a "course of conduct"? How do you prove a "course of conduct"? You don't have any accounting provisions? We are getting rid of accounting provisions and "reasons to know." We are going to replace that with "course of conduct"?

Mr. UNGER. I think you would find course of conduct would be, for instance, if a man in a transaction is saying one thing and winking at the same time or shaking his head as though he doesn't believe it. A course of conduct can be a modus operandi in business to get around bribery laws. Course of conduct can be defined.

Mr. WIRTH. Shaking one's head does not get defined in a statute. It does not get defined in a legal proceeding.

Mr. UNGER. It would be in legal proceedings. It becomes an issue of fact.

Mr. WIRTH. "Course of conduct" is a definable area where "reason to know" is not?

Mr. UNGER. Yes. That is my judgment, and it is an issue of fact that I would feel much more comfortable proving in court.

Mr. WIRTH. Mr. Johnston, do you have any comment on that?

Mr. JOHNSTON. Yes, I would just like to say that in the case that Mr. Unger referred to, in which the British Monopolies and Mergers Commission was looking at the case of an American company that was trying to buy out a British company, the opinion given by the Commission referred to "reason to know," and they said that

because of the ambiguousness of the "reason to know" standard this particular American firm has been especially cautious. The manifestation of that cautiousness is that they have refused to hire certain kinds of agents.

We think that as a result of that, this firm is passing up the chance to do legitimate business. I just give you that as an example of somebody else's opinion that the "reason to know" standard is difficult to define.

Mr. WIRTH. Does "course of conduct," which is a replacement on the Senate side, for "reason to know," have a legislative history? Do you know, Mr. Unger? Does the statute define what we mean by "course of conduct"?

Mr. UNGER. I don't know the answer to that but I am comfortable in guessing that it does, yes.

Mr. WIRTH. Could you submit that to us?

Mr. UNGER. Yes.

Mr. WIRTH. We would appreciate it. We have been looking for it and haven't been able to dig that out anywhere.

Mr. UNGER. I will look and see if I can find it.

Mr. WIRTH. To pin down the ambiguities. I agree if legislation is ambiguous, let's clarify it. But let's not create yet other ambiguities.

Mr. UNGER. I agree with the chairman.

Mr. RINALDO. Will the chairman yield?

Mr. WIRTH. Yes.

Mr. RINALDO. I think that is another good point. It is defined in the report, but that is an area where during markup I want to assure you I would be very pleased to work with you in clearing up that particular point.

Mr. WIRTH. "Reason to know" is defined in 29 other statutes. It has a legislative history. We would like to know if "course of conduct" has the same agenda.

Mr. UNGER. Mr. Chairman, if I may offer a correction, it is included in the statutes. It is not defined.

Mr. WIRTH. It is used and there is a legislative history related to the "reason to know." If it is ambiguous, let's look at it. We ought to understand what is involved here.

Mr. RINALDO. Mr. Chairman, for your information they define it on page 17 of the report. They say,

The committee intends the term "course of conduct" used with the term "authorized" in section 104(b) to refer to those situations where a company through its words or courses of conduct, has intended that a corrupt payment be made.

For example, a company's refusal or failure to respond to an agent's suggestion or request that a corrupt payment be made would violate this section as would a company's continuing employment of an agent known to the company to have made corrupt payments in the preceding 2 years in violation of applicable United State laws or those of the country in question.

While it is defined there, I am sure if you and I get together we can do an even better job.

Mr. WIRTH. It is fascinating that the "course of conduct" is used as a way of defining what "course of conduct" means.

May I ask you, Mr. Unger, the same questions that I asked of Ambassador Brock. The language in the Senate bill says that "any expenditures including travel and lodging expenses associated with

the selling or purchasing of goods and services or with the demonstration or explanation of product" shall not be covered by the act. Is that a provision that you think is supportable?

Mr. UNGER. I think it is supportable. I heard you quote Mr. Rose as saying he had some question about it from the Department of Justice. I don't remember that in his prepared testimony.

Mr. WIRTH. That was not in his prepared testimony. Mr. Rose made this statement during the question and answer portion of our last hearing. We would like your response also.

Mr. UNGER. My response is it could be made a little more precise.

Mr. WIRTH. Anything can be an expenditure associated with selling goods and services—anything.

Mr. UNGER. I agree it could be made more precise. My understanding of those words is they were a compromise on the Senate side of varying interests, and I am sure that they can be improved.

Mr. WIRTH. The other question—and I ask you to respond to this as well—regards subsections (a) and (b), which are the anti-bribery provisions.

The Senate states that these provisions—

* * * shall not apply to any ordinary expenditures including travel and lodging expenses associated with the performance of a contract with a foreign government or agency thereof.

It seems to me that these kinds of exceptions negate the effect of the entire act, and can create even greater confusion and uncertainty.

Mr. UNGER. I will agree it could create additional confusion and uncertainty and it could be made more precise.

Mr. JOHNSTON. Mr. Chairman, could I make a comment on that? If you go back to the law that we are suggesting be amended, the wording that exists right now is "payments to employees of foreign governments whose duties are essentially," and I quote, "ministerial or clerical." Now, to me, that goes all the way from the top to the bottom. It doesn't define anything. It is true that this language, it seems to me, can be improved, but it is hard to get more confusing than that other language.

Mr. WIRTH. Let me ask you about another section of the Senate bill, Mr. Johnston, which relates to our responsibilities to other governments. In your testimony you state that "The Foreign Corrupt Practices Act affects legitimate business transactions in and among other things, the lack of flexibility to provide legitimate gifts."

As you know, the recently passed Senate bill, under an exception to the bribery provisions, would permit "any payment, gift, offer, or promise of anything of value which constitutes a courtesy, a token of regard or esteem or in return for hospitality."

Do you think that that is an appropriate change to be made in the language of the legislation?

Mr. JOHNSTON. Mr. Chairman, I think you can make a change like that without getting into the question of the massive kinds of bribery that we were talking about or that the country was talking about in 1976 and 1977. What was being talked about at that time were payments of several million dollars. Now, it is hard for me to

believe that this kind of definition would strike at the heart of the bribery provisions. I think it is clearer, yes.

Mr. WIRTH. How does a watch fit into the situation of a gift?

Mr. JOHNSTON. I think that we would have to have the opinions of lawyers on some problems, but I don't think it would be possible to think about gifts which are defined in this fashion as being the massive kind of bribery which the law was set out to stop.

Mr. WIRTH. Let's just look at the situation.

Mr. JOHNSTON. Mr. Chairman, could I say something?

Mr. WIRTH. Let's look at a watch versus Lockheed. There is obviously an extraordinary amount of symbolism involved in these episodes. Not only is gift giving to public officials of great concern to the people in this country, but we saw what happened with the Government of Japan and what happened to a government in Italy, and most recently, what has happened, very unfortunately, here. Other countries are equally concerned about this.

Relating to gifts, we asked the Congressional Research Service to give us a picture of what other countries said about bribery laws and gifts. A great majority of foreign countries include the accepting of gifts under their bribery laws and provide substantial jail sentences and penalties for public officials who accept gifts. I won't read the whole list, but let me give you some of them in alphabetical order.

Prohibitions against accepting gifts appear in the laws of Argentina, Bolivia, Chile, Colombia, Costa Rica, Denmark, Dominican Republic, Ecuador, Egypt, El Salvador, France, Greece, Guatemala, Haiti, Honduras. They say it is against their laws to accept gifts. On the other hand, the Senate bill says it is perfectly appropriate to allow gifts to be given to public officials. How do you reconcile the proposed changes in our laws with the laws of other countries?

Mr. JOHNSTON. Mr. Chairman, you realize, of course, that we are the only country that has tried through such an act to get at bribery extraterritorially. There is no other country whatsoever, that has tried this way and this, of course, brings certain amount of trouble. One of the features which we like in the current bill which the Senate has passed is the clear statement that if a transaction is legal in the country in which it takes place, it would be accepted as permissible under this act.

Mr. WIRTH. As you pointed out, maybe no other country has an antibribery law with this kind of reach. Do you know of any other country whose companies were involved in bribery and thereby brought down a foreign government?

Mr. JOHNSTON. I beg your pardon?

Mr. WIRTH. Do you know of any other country whose companies have bribed and thereby helped bring down foreign governments?

Mr. JOHNSTON. I do not, but I am almost positive they exist.

Mr. WIRTH. I was just wondering. We are very familiar with that, and that was the initial reason for this legislation—the very unsavory behavior that the people in this country didn't want us to be involved with. Allegedly, there is some idealism left in what the country is all about and what we ought to stand for both at home and abroad.

Mr. JOHNSTON. That is right.

Mr. WIRTH. It seems to me a little bit disingenuous to say that no other country has a similar law, when no other country is as deeply involved around the world as we are. No other country views itself as one that still has a set of ideals that it wants to transmit not only at home but around the world.

Mr. JOHNSTON. I am not sure that other countries would agree with you in that interpretation, but I wouldn't try to speak for them.

Mr. WIRTH. What does that mean?

Mr. JOHNSTON. Well, the implication of what it seemed to me you were saying was that we were the only country that had ideals, I don't think that there would be other countries—

Mr. WIRTH. I am saying that there are ideals that we are trying to transmit and there are still some who think that it is important to do so.

Mr. JOHNSTON. As long as it can be done with a clear law which doesn't stand in the way of our exports, I think we all agree with that.

Mr. WIRTH. Let's keep in mind, do we take our standards from other countries any more than as we were discussing earlier, from what may or may not be good legislation written elsewhere, or do we set higher standards. It seems to me that that is something that this country has always been about, attempting to set that kind of very clear and high standard.

Mr. David Newsom, former American Ambassador to Libya, Indonesia, and the Philippines, and former Assistant Secretary of African Affairs, recently submitted a statement to the subcommittee in which he stated, "American businessmen often ask, 'Why us?' Why should the Americans be singled out for restrictions when all around them their competitors appear to operate without such restriction?" That is the thrust of much of what has been said this morning.

And Ambassador Newsom responds:

In my view, it is a fact of international life that the corrupt association of a major American company with a foreign official carries political implication that relations with other foreign companies do not. We cannot escape our political involvement as a major power. Our companies cannot escape the fact that their activities will never be totally detached from local sensitivities relating to U.S. intervention of any sort in the internal affairs of another country.

Would you agree that Americans have a special role, as Ambassador Newsom has suggested?

Mr. JOHNSTON. I think so, because of our global reach. However, I think the quotation that you have just read is one which is generally accepted by most of the people, that the United States should not be condoning bribery abroad. The question, it seems to me, that we are facing is, Is the current text of the act accomplishing what it is supposed to do at a sufficiently small cost to the country?

Mr. WIRTH. Then let's keep the focus on that. Again we get into the argument where we hear all the stormy set of numbers about exports, the fact that there may be problems with exports and that this is because of the Foreign Corrupt Practices Act. I don't think the data shows that the FCPA is the No. 1 inhibitor of exports and that we shouldn't have a piece of legislation because other countries don't do it.

The purpose of reading the statement of Ambassador Newsom was to show that we do have a special role. Regardless of whether other countries have extraterritorial bribery laws, there is a special role that we play in this country. So focusing on the legislation, it doesn't seem to me, as one Member of the Congress has argued, is that we shouldn't do it because other countries don't do it.

Mr. JOHNSTON. We are not making that argument. I don't think there is anybody in the administration who claims that we are trying to get rid of the Foreign Corrupt Practices Act. What we are trying to say is let us clean it up in such a way that it will still stand in the way of bribery and will not cause unnecessary impediments to our exports. I think that is essentially what we are trying to say.

You raised the question of whether this is the No. 1 impediment to our exports. I would hate to try to make a judgment on what is the single most or the second most or the third most important impediment, but it seems to me that when we have gotten so many complaints from businessmen that there is a problem in this law—not related to the antibribery aspects, but to the definitions and to the ambiguities in it—that it is time we should really pay some attention to it. It may not be No. 1 or No. 2 or even No. 3, but it still is worth paying attention to because of the importance of exports to this country.

Mr. WIRTH. The taxpayers don't elect to pay their taxes either, but because you get complaints from taxpayers doesn't mean that you eliminate the 1040 form and the requirement that people ought to pay taxes.

Mr. JOHNSTON. I am not saying that we are seeking to encourage bribery. What I said was that is when a businessman says that the law is confused, when you get examples such as Mr. Unger has quoted here where lawyers are not willing to give opinions, when people say that the situation is ambiguous, I think we ought to listen to them and try to improve the act.

Mr. WIRTH. Let's talk about where that ambiguity is; let's separate it out from the bribery situation. Let's separate it out from all of the very loose rhetoric about the extraordinary problems this causes, for example, the figure of \$1 to \$2 billion—undocumented but that figure keeps being used—80,000 jobs being used over and over and over again, undocumented, 19 cases presented by the USTR submission—the chamber has destroyed the evidence for 7 and the other 12 came on the basis of the telegram we discussed earlier.

We have 19 cases held up as if they are the greatest documentation in the world. It is very hard to take that credibly. The GAO report is referred to over and over again, in which the GAO says the FCPA is ambiguous. The Carter administration report of 1980, is held up as evidence. The Justice Department wouldn't support this report. Again, the evidence of ambiguity it is an awfully loose operation. We are trying to pin down what it is that companies want to do. And we do want to not just increase the number of ambiguities.

Mr. Rinaldo.

Mr. RINALDO. I want to commend the chairman for his thoroughness in this hearing this morning. It indicates to me, when he cites

the examples not only in the legislation that passed the Senate but the examples in the current law, that we have a big job ahead of us in this committee. I want to once again give you my very strong assurance that I want to work closely with you, and would hope that we would have hearings as quickly as possible, so that we can move on to a model piece of legislation that I am sure the Senate, the administration, businessmen and businesswomen, antibusinessmen and antibusinesswomen, and everyone in this country and in foreign countries would hold up as a piece of legislation that they can look to with the greatest amount of respect, and can interpret with the ease and simplicity of a person in high school.

What I would like to know, since we have discussed all these different areas, is do you feel—and I would like to ask this particularly of Mr. Unger—it is your position that the FCPA has a particularly great impact—we are talking about people already in business. How about small businesses who are trying to get into the export market? I don't know how much government money we spend telling people to begin exporting.

Do you think this is a disincentive as it now stands? I am talking not about the big multinational corporations but the small businesses that would like to get into the export business.

Mr. UNGER. My response to that question is an unqualified yes. It is a disincentive. It is strange for the lawyers. It is fearsome for the small company that wants to get started, and they stay away. Generally, exporting is a marginal increase in the beginning, and the risk is great.

What if your company is held to be liable for breaching a foreign corrupt practice? That is not going to help your business, so what you do is stay away from it.

Mr. RINALDO. I don't understand, I wish I had the ability to bring before this committee—how do you find out? I have friends of mine who say they don't want to export. They are in business, and they mention this act. But how do you know how much business they are losing by not getting into it?

I don't know how we could quantify that, but I appreciate your response, and would like to follow up with this question. Would you describe for us some of the difficulties that small business in particular must face in complying with the terms of the act as currently written?

Mr. UNGER. First of all, most small businesses aren't acquainted with agents they might be dealing with. They are learning how to get into the export business through strangers or referrals from other people. The act is vague. The act is unclear. It subjects them and their counsel to a review after the fact, on a course of conduct where somebody can come in and say, well, this happened, that happened, this happened and that happened, and you had a reason to know after these events happened that you were breaching the act.

A lot of the conduct is in a foreign country with strangers. The small businessman will stay away until we can write a law that is definitive, so he knows where he is going, he knows what he is doing, and he feels comfortable in expanding into the export trade. Now, I think it is possible to do that, and I would offer the resources of our office to help in any way possible.

Mr. WIRTH. In other words, what you are saying is that we can write a law that will achieve the same results as the legislation currently written, that is, effectively prohibit bribery, yet be easily understood, be complied with, and not be a disincentive to small businesses attempting to enter the export field, to companies already in the business, and to large corporations as well?

Mr. UNGER. Yes, sir. I hope we are creative enough to accomplish that, and we should be.

Mr. RINALDO. I would hope so.

Mr. WIRTH. Will the gentleman yield?

Mr. RINALDO. Yes.

Mr. WIRTH. On the point regarding our creativity and our ability to look at language, Assistant Attorney General Rose, who was up here for the oversight hearings 2 weeks ago, agreed to submit to us their analysis of the Senate language—what they thought was clear, what was not clear, what was enforceable, what was not enforceable. Would it be possible for the Commerce Department and the State Department to do the same?

Mr. UNGER. I am not certain that we have an enforcing responsibility, nor should I enter that part of it.

Mr. WIRTH. You are telling us that the language is ambiguous but you are not going to come in and tell us what—

Mr. UNGER. No, that is not what I am saying. I am saying, Mr. Chairman, that I am willing to tell you what is clear and what is not clear. I am not equally willing to say what is enforceable or not enforceable. That falls to the Justice Department.

Mr. WIRTH. We have been told how ambiguous the previous language is.

Mr. UNGER. I will be glad to address the language.

Mr. WIRTH. I have pointed out at least four areas that I think are very troublesome in the language on the Senate side.

Mr. UNGER. I would be pleased to address the language and its clarity.

Mr. WIRTH. Would it be possible for you or the State Department to do that as well, Mr. Johnston?

Mr. JOHNSTON. You are asking for our judgment on the adequacy of the Senate's language; is that right?

Mr. WIRTH. Yes, how clear the Senate language is. We want to separate out the antibribery disincentive from the ambiguous language disincentive. I hear that nobody wants to bribe. We have all agreed on that, I hope. Is the language on the Senate side clear; does it provide the nonambiguous language that you consider necessary from your experience, having sent out all those telegrams to people and having a data base in the State Department regarding how many problems the FCPA causes? Since you must know a lot about how to clarify the act, could you look at the Senate language and help us to examine if the Senate language does the job or doesn't do the job, and if not, how it might be changed?

Mr. JOHNSTON. Right, I think we would like to submit a consolidated reply with the Commerce Department. I don't see much point in—

Mr. WIRTH. Actually, what we would like to do, if we could get it, is a separate submission. It is also nice to know accountability as we talk about this act. One of the things we do on a steady basis is

squeeze a sponge and the water comes out one end and then out the other. We would very much like to hear from you based on your firsthand experience and on the data you have collected.

Mr. JOHNSTON. We guarantee you will have a signature at the end of it for accountability.

Mr. WIRTH. Could we have comments do that from the Departments of State and Commerce, by January 15, or February 1?

Mr. UNGER. Sure.

Mr. WIRTH. You can tell us what would be useful.

Mr. UNGER. Yes.

Mr. WIRTH. Mr. Rinaldo used the word creative. I think there are a variety of issues here.

Mr. UNGER. I would be pleased to try my hand at it.

Mr. WIRTH. USTR—Mr. Maroni is here, I see. Is it possible for you to provide that for us from USTR?

Mr. MARONI. By January?

Mr. WIRTH. By January 15. Deadlines are tough but we are all interested in getting a handle on this.

Mr. UNGER. I would prefer the February 1 date.

Mr. WIRTH. Let's move the date to February 1 if that is better. Is that all right, Mr. Maroni? Can we do that?

Mr. RINALDO. Mr. Chairman, that is an excellent comment you just made, and the request is very good. Why don't we do this? In order to expedite the process perhaps we should get some members together, introduce the Senate bill, over here, and then we can use that bill as a vehicle and get their suggestions and improve it to the point where it will be the kind of legislation that you and I would be very, very proud to go out on the floor and vote for and vote for in this committee. In that way we will have it in a regular hearing on a specific piece of legislation, and we can rip it apart, we can improve it, and I am sure we can come up with—

Mr. WIRTH. Mr. Rinaldo, any member of the subcommittee can introduce a piece of legislation anytime he or she wants to.

Mr. RINALDO. It is only the chairman who can call a hearing on a particular bill.

Mr. WIRTH. That does happen to be the situation, doesn't it?

Mr. RINALDO. And I can tell how anxious you are by your previous comments.

Mr. WIRTH. Mr. Rinaldo, let's be very clear. Looking at the Foreign Corrupt Practices Act, I have said let's not rush to judgment.

Mr. RINALDO. We are not doing that.

Mr. WIRTH. As I said earlier, on the Senate side they rushed in with that initial bill which they said was just absolutely the best thing they could do, and that changed. We now have another piece of legislation. Even the Department of Justice says that the Senate bill presents a lot of ambiguities and raises a lot of issues on which the Justice Department would like to comment. We are still finding out what is evidence, and what is not evidence. We are exercising the oversight that is one of our responsibilities.

A lot of people run around saying: What are you trying to do; are you delaying the legislation? Are you trying to do this or that?

We also have a responsibility for oversight to see if the act works or doesn't work. That has not been done anywhere. It wasn't done on the Senate side. It has never been done on the House side. I

think with your pushing and help, we have done a very responsible job of looking at this legislation, what is real and what isn't real. We have exploded a lot of the myths and have separated out the issues that are most important from those that are unrelated. That is a very helpful thing to do. That is one of our responsibilities. On February 1 we will look forward to hearing from all of you and we greatly appreciate your assistance.

Do you have anything else?

Mr. RINALDO. Yes, I want to make it clear, first of all, I never said the original bill shouldn't be changed, as you know, in our public and private conversations. I have always said I was amenable to amendments there. I am amenable to amendments in the Senate bill, but I think that in addition to that oversight function, which is so vitally important, we are also exercising the legislative function. We have to have something here so that the people who are going to do all this work and come up with the suggestions, revisions and improvements, have a specific vehicle that they can take a look at.

What I am really saying, Mr. Chairman, is maybe we should handle—maybe that is the same way as handling the telecommunications bill. My understanding on the telecommunications bill is—and correct me if I am wrong—you put it in so that we have hearings and we have the specific vehicle that we can change or revise or amend, but that you are not wedded to the language in the specific bill that you put in. Is that correct?

Mr. WIRTH. I am sure that there are changes that have to be made in that language. I have no question about that. As I indicated to the gentleman from New Jersey earlier, it is very simple to introduce a piece of legislation. There is a small hopper on the floor of the House into which you drop a bill.

Mr. RINALDO. I am very familiar with that.

Mr. WIRTH. The bill will get to the subcommittee and we will review it. I would very much like to receive the comments of the State Department and the U.S. Trade Representative and the Justice Department, and try to understand what it is we are talking about. One must also be very careful about creating flatcars in this world that go rolling away loaded up with all kinds of nonsense. We don't want that to happen here. The gentleman from New Jersey, I know, wouldn't want that to happen.

Mr. UNGER. Mr. Chairman, if I can get my comments in earlier, I certainly will.

Mr. WIRTH. Terrific, Mr. Unger. What a delight.

Mr. RINALDO. One more question before we close that I would like to ask the witness, and I want to assure the chairman maybe I will put a bill in and over the Christmas recess I am sure with the yuletide spirit—I know where the little box is. I know how to drop it in, but I have great difficulty finding out how to get you to hold a hearing.

Mr. WIRTH. Would the gentleman yield?

Mr. RINALDO. Yes.

Mr. WIRTH. We have held hearings as announced, and scheduled those very well. If the gentleman wants to work on legislation, let me assure him that the staff resources on the majority side will be at his disposal if he wants to use them.

Mr. RINALDO. Very good. I may take you up on that offer. I know the witnesses have been here for quite some time.

I just want to ask one final question of Mr. Johnston. In the report from the Foreign Service that was alluded to earlier and included in your testimony, reference is made to the reluctance of American companies to provide details of lost business or forgone opportunities to embassy officials, to us, to anybody. Really, this is what we have been debating ad infinitum. Why can't we get more hard evidence? Could you explain from your vantage point why American companies are reluctant to come forward with this information? And also the second part of my question is, Isn't it difficult to assess in a quantitative way the effect of the Foreign Corrupt Practices Act?

Mr. JOHNSTON. To answer the second part of your question first, I don't see how it is possible to decide what might be.

Mr. WIRTH. Would the gentleman yield?

Mr. JOHNSTON. What the possibilities were.

Mr. RINALDO. May we have the answer?

Mr. JOHNSTON. I just don't understand how a person could decide what might have happened if somebody had felt he was free to do something.

In regard to the first question, I think part of the reason is that the law itself is vague. A businessman may have an opinion on where he thinks the law stops, but he doesn't know whether the Attorney General has that same opinion on where the law stops. And, his lawyer may not be too precise on where the law stops. So the businessman comes saying that if he had been able to entertain a man at a meal, or if I had been able to fly him over to look at his plant, he might have been able to make a sale. But if somebody else comes to the opposite judgment, that the act indeed was on the other side of the line, then the businessman is in really sort of a bit of a fix, it seems to me.

The other thing that makes it more difficult for businessmen to give examples is that they have to identify countries and officials and acts they would like to perform, but these people want to keep on very good terms with the officials in the country in which they are dealing. They don't want any allegation that there is anything wrong. They don't want any allegation that they are engaged in anything close to improper conduct. I think that is the reason that we have the greatest difficulty.

Mr. RINALDO. I want to thank both of you. You have been very patient, and your testimony will certainly help provide, the basis for the kind of legislation that the chairman, myself, and the other members of this committee would be very proud to vote out of this committee once we finally get it worked out.

Mr. WIRTH. Just on the first part of that question, you said it is very, very hard to document and pin down a figure. Would that then suggest that we ought to strike from future discussions of the subcommittee all reference to 1 or 2 billion dollars' worth of lost trade or 80,000 jobs, which numbers have been bandied about in this room and in the testimony previously? Would that be a fair result of what you just said?

Mr. JOHNSTON. Mr. Chairman, I like that question, because what you imply is that you will take the word of the State Department

on what ought to be going on in the subcommittee. I don't know that anybody has ever done that before. I have not used \$2 billion or \$1 billion. Had I thought I had a figure that I would like to support, I would have put it forward. If somebody else wants to put forward a figure and support a figure, I think you ought to listen to his reasons.

Mr. WIRTH. What would your reaction to that be, Mr. Unger? I appreciate the fact that you have not loaded your testimony with a figure like this one, Mr. Johnston, a very careful State Department advancing our interests around the globe. Thank you, sir.

Mr. UNGER. I hope you will note the Commerce Department hasn't advanced that either in testimony.

Mr. WIRTH. Would that be all right if we just leave that out of the discussion and no longer talk about the \$1 to \$2 billion? We have agreed it is very difficult to document it. It seems to me that is a logical consequence of our discussion.

Mr. UNGER. I would be willing to say that the number of jobs and the amount of money must be enormous, but I don't know how to measure it.

Mr. WIRTH. Enormous. It could be \$4 billion and 150,000 jobs.

Mr. UNGER. It might be.

Mr. WIRTH. It might be the equivalent of all of our oil imports.

Mr. UNGER. I don't know about that.

Mr. WIRTH. Thank you very much.

Mr. UNGER. I am not sure I want to go that far.

Mr. WIRTH. We really appreciate your being here. You have been very helpful and we will look forward to hearing from you.

Mr. UNGER. Thank you.

[Whereupon, at 12:20 p.m., the subcommittee adjourned.]

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FOREIGN CORRUPT PRACTICES ACT— OVERSIGHT

TUESDAY, JUNE 8, 1982

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON TELECOMMUNICATIONS,
CONSUMER PROTECTION, AND FINANCE,
COMMITTEE ON ENERGY AND COMMERCE,
Washington, D.C.

The subcommittee met, pursuant to call, at 9:50 a.m., in room 2322, Rayburn House Office Building, Hon. Timothy E. Wirth (chairman) presiding.

Mr. WIRTH. The subcommittee will come to order.

This is the fourth oversight hearing by this subcommittee on the Foreign Corrupt Practices Act. It is, in my view, the most important hearing we have had on this subject.

The purpose of today's hearing is to fully examine the problems American businesses have had operating under, and complying with, the Foreign Corrupt Practices Act. I cannot overemphasize the importance of the testimony of the witnesses before us today.

This subcommittee has spent a great deal of time reviewing the act, its purpose, its implementation, and its impact on our export performance.

When we were approached last year by groups who supported amendments to the act, we decided that it first might be a good idea to question whether we even needed a law prohibiting overseas bribery by American companies.

We focused our first hearing on that question. Witnesses agreed that it was important, for American national security, foreign policy, and other public policy reasons, to have such a prohibition against bribery, even though no other country in the world has such a law.

Before the act was passed, more than 400 companies disclosed questionable payments totaling more than \$300 million. After the act became effective, there was, by all evidence, a dramatic decline in the disclosures of bribery by American companies.

At our second hearing, we explored, in depth, the enforcement record of the Securities and Exchange Commission and the Department of Justice.

We found no record of prosecutorial abuses. Indeed, the SEC and the Justice Department have each brought only two cases under the bribery provisions of the act, and only one of those cases was a criminal prosecution.

Sixteen civil actions have been brought by the SEC alleging violations of the accounting provisions, but each of these cases involved violations of other provisions of the securities laws, such as the antifraud provisions.

At our third hearing, we sought information about the impact of the act on American export performance. Although overall export sales had increased dramatically during the years after the act was passed, we wanted to learn if the Foreign Corrupt Practices Act had had any effect on U.S. exports.

We were extremely frustrated by administration officials who continued to want to blame our balance-of-payments problems on the Foreign Corrupt Practices Act, while neglecting to mention the dramatic increases in the price of imported oil and our continuing dependence on foreign oil.

Those same officials even today seek to blame recent export declines on the act, without mentioning the effects of current high interest rates—a factor which everyone agrees is far more significant to our overall export performance.

So it was somewhat disingenuous for the administration to want to blame the Corrupt Practices Act.

For that reason, I determined that it would be far more useful to talk with individual business people who had had problems operating under the act.

Over the past several months, the subcommittee staff, at my direction, has contacted a number of companies in an effort to learn their specific problems in conducting their overseas operations in compliance with the act.

A number of companies have told us that certain provisions of the Foreign Corrupt Practices Act are unclear and the language is fuzzy.

We have been told that some American companies have been forced to forgo legitimate export opportunities because they are confused about what conduct is permitted and what conduct is prohibited under the act.

When the Foreign Corrupt Practices Act was passed in 1977, it was acknowledged that some business would be lost because of its prohibition against bribery. However, it simply is not in our national interest—nor is it fair—for American companies to forgo legitimate export opportunities because they are uncertain about what the law requires.

That is really what we want to focus on, what is the language, how can we focus it to make it more certain, but yet not introduce further ambiguities into the law.

We have invited a number of companies to testify at our hearing. Although many were reluctant to testify, some agreed to appear and are here today, and others have agreed to submit statements for the record.

We have asked these witnesses to discuss their export experiences, to detail the problems they have had in understanding the Foreign Corrupt Practices Act, and to identify provisions of the act they believe are unclear.

Finally, we have asked them for suggestions on any changes they believe should be made to the act.

I appreciate your appearance before this subcommittee. I am hopeful that this will be a productive hearing for everyone involved, and I look forward to working with each of you on this important issue.

Let me add a procedural detail as well. The Speaker has called a session for 10 this morning on the budget. As a member of the Budget Committee, I will have to be engaged in that as we try to struggle to find the makings of a budget which is so terribly important for the economy and for the country.

Rather than delay the hearing, I have asked Congressman Swift, who has been deeply involved in this issue, to chair the hearing during that 45-minute-or-so time period in which I will be gone.

Gentleman, thank you for being here. Before beginning, let me ask my colleague from the State of Texas, Mr. Collins, if he has any comments he would like to make.

Mr. COLLINS. Thank you, Mr. Chairman.

We welcome our guests with us today. This is the fourth and last of our scheduled oversight hearings on the Foreign Corrupt Practices Act. They began last autumn and since we started, the Senate approved S. 708. That bill would provide a wide-ranging reform of this law.

I believe the testimony we have heard thus far is almost unanimous in calling for changes similar to those passed by the Senate.

These changes address serious problems that have arisen from compliance with this law. At the same time, the principal purpose of the statute is preserved, that is, to prohibit bribery of foreign government officials by U.S. corporations.

I am pleased today that we are hearing from the business community and from companies who can tell us firsthand about their experience in dealing with this FCPA. I am sure you will be able to provide us with the valuable information.

I want to reiterate the readiness of the Republican members of the subcommittee to work with the chairman and other interested members in drafting legislation to address the widely recognized problems which have arisen under the FCPA.

More than a year ago, I cosponsored a bill, H.R. 2530, along with several members of the subcommittee. I am not limited to any particular approach, but I want us to approve a bill this session.

Loss of American exports, and American jobs, are among many reasons to reform this law. I feel very, very strongly about it because as I understand it, no other country in the world has any type of punitive legislation such as we have imposed on the businesses in our country, and we do have an unfavorable balance of trade.

The main concern in our country today is to lower interest rates and increase jobs for Americans.

It would be a tremendous step forward if in our legislative process we could come out with a House bill.

I feel sure we will, because there is tremendous interest and concern in our committee.

Thank you, Mr. Chairman.

Mr. WIRTH. Thank you, Mr. Collins.

Our first panel this morning, a distinguished trio, Mr. Shaw Mudge, president of Shaw Mudge & Co., Stamford, Conn.; Mr.

Eamonn McGeady, president, Martin G. Imbach, Inc., Baltimore, Md.; and Mr. Bernard Featherman, president, Western Steel Co., Philadelphia, Pa.

Gentlemen, thank you very much for being with us and for your patience and help with the subcommittee on this important issue.

Perhaps we could begin with you, Mr. Mudge, and go to Mr. McGeady and Mr. Featherman. I think you know the rules of the subcommittee. Your statements will be included in the record.

I think it would be useful if you would summarize your statements and then react to what the others have said. We then will have time for questions and answers and get into a discussion rather than dwell on the kind of formalities that seem too often to smother deliberations of this august institution.

Mr. Mudge.

STATEMENTS OF SHAW MUDGE, ON BEHALF OF NATIONAL SMALL BUSINESS ASSOCIATION AND ALSO SMALLER BUSINESS ASSOCIATION OF NEW ENGLAND; EAMONN McGEADY, PRESIDENT, MARTIN G. IMBACH, INC.; AND BERNARD FEATHERMAN, PRESIDENT, WESTERN STEEL CO.

Mr. MUDGE. Thank you, Mr. Chairman, Mr. Collins.

You would rather have us not read our testimony?

Mr. WIRTH. Do what you are comfortable with. We will include it in the record. Hit the high points and what you think the main themes are and that would be fine.

Mr. MUDGE. The outline of my testimony is a comparison of the cultural diversity of the East as opposed to the technological traditions and the ethical traditions of the West.

I dwell at some length about those differences to try to put into perspective the history that has led to the legislation we have to contend with, particularly small business persons.

The Chinese, for example, for several thousand years, had the concept of scholar-officials, which is a nonheredity autocracy.

Very often, the villages pool resources to send an aspiring person to the central cities and there, if he did well in the civil service exams—China was the first to have such programs—he would then rise to what in the Chinese culture was the highest level of work which is public service.

Now, as they rose, they were expected to repay their obligation and their debt and the cost of their education back to their communities.

That is dwelled on here and that's the background of Confucianism and its relation for 2,000 years to the Chinese thinking.

My name is Shaw Mudge, president of a small fragrance and flavors firm in Stamford, Conn. We employ 44 men and women. I am also president of a small herring company in Harrington, Maine. Six people are directly employed by Pineo Point Fisheries. My third small business, Columbia Air Services, is an FAA-approved airplane maintenance operation with nine employees working in New London, Conn. All my small businesses are involved, to a limited extent, in international trade. We'd like to increase our overseas sales.

One of my hobbies is the study of American history. Perhaps it came about because my family has been in the fragrance business for four generations and we had to travel worldwide to purchase essential oils. Or perhaps it's just that I am proud to be an American and I enjoy studying the history of America's growth and expansion. One area of particular interest to me is East Asia. Studying United States and China from a historical perspective offers a better understanding of the cultural differences between East and West.

While America was a colony, we had no choice but to trade exclusively with Great Britain. But in 1784, within a year after Cornwallis' defeat at Yorktown, Robert Morris sent the "Empress of China" from New York to Canton, China and back. Her voyage returned a profit of better than 25 percent.

Although America was late in entering the East Asian market—after England, France, Holland, and Russia—China had long established the tribute system for dealing with foreigners. Or as they called us, "barbarians."

Now China had some basis for feelings of superiority. China was unified in 220 B.C., and was ruled by the same family of emperors until 1912.

With the emperors came a common written language and a system of viable ethical standards, known as Confucianism. Just last month, the cover story on Far Eastern Economic Review was "Singapore's Lee Kuan Yew, the Modern Confucius," subtitled "Economically Successful Singapore Becomes More Inward Looking, Searching for a Soul."

The May 20 report of the same story in the New York Times says, "Confucianism is a humanistic ethical philosophy rather than a religion."

Confucianism, the ideology that prescribes proper behavior or correct conduct, was China's social and political cement for 2,000 years,

Japan, Korea, and Vietnam also were influenced by Confucianism. Chinese students spent many years immersed in the pursuit of Confucian classics. They learned correct behavior between parents and children, husband and wife, neighbor and neighbor, ruler and subject, as well as proper conduct between host and stranger.

Scholars were tested in the Confucian classics through the famous examination system—a Chinese invention. All outstanding scholars were eligible to compete in the examinations.

It was not unusual for a village or clan to pool their resources to support a local genius. Those men who were especially proficient rose through nine ranks of Civil Service.

They became scholar-officials, a nonhereditary autocracy. They supported the emperor, whose Confucian-prescribed conduct was government by goodness; government by the moral prestige of the ruler.

A quotation attributed to Confucius says, "When the ruler himself does what is right, he will have influence over the people without giving commands. When the ruler himself does not do what is right, all his commands will be of no avail."

While the family of Emperors remained constant in China for over 2,000 years, the autocracy of scholar officials also remained constant.

In contrast to Europeans who came and went, the scholar-official bureaucracy remained the key to running the Empire.

Within China's Confucian cultural hierarchy, merchants were considered lower class. They could not receive an audience with the emperor. So the scholar officials awarded Chinese merchants certain posts where they could receive foreign merchant barbarians.

Not just foreign merchants were considered barbarians, but all foreigners were called barbarians by the Chinese. No other nation had achieved China's cultural superiority which developed from their Confucian ideology.

Nevertheless, the Emperor, secure in his position, was extremely magnanimous. His benevolence extended to all foreign governments as long as their representatives practiced prescribed conduct.

Imperial benevolence meant not only lavish gifts, but inevitably, access to Chinese markets and merchants.

So while the merchants were left at the point of entry "to do excellent business" with their Chinese counterparts, their foreign leaders proceeded to Peking to perform the formalities.

Among these was the famous athletic feat of kowtow—three kneeling and nine prostrations or head-bangings in the Emperor's presence.

The tribute system was considered mutually beneficial. It reassured the Chinese of their superiority and benevolence and at the same time, of the barbarian's proper submissiveness.

It lined the palaces of the barbarian rulers with Chinese luxuries. And it lined the pockets of barbarians and Chinese Hong merchants with cash.

By 1760, well before the first Americans arrived, the trade at Canton, the western barbarians' port, was systematized. European merchants dealt with their assigned Chinese merchants.

In fact, Americans never performed tribute to Peking. By 1784, the French and English were becoming testy about the procedure.

But more significant, Americans never performed tribute because the early American Government left trade to America's entrepreneurs. The East Asia trade remained for many years a young man's trade with young men's profits. Profits requiring daring and innovations.

As more trade came to China, commission houses sprung up, assigned by scholar officials and controlled by the comprador or Chinese go-between.

He was a multilingual interpreter and treasurer for Chinese accounts. He was also in charge of the Chinese staff.

All hiring and firing was done by him in the treaty ports. Compradors solved the endless problems caused by Chinese irregular weights and measures, and, by Western standards, the less predictable business ethics.

Understandably, it wasn't long before China wanted to stop the sale of opium, and the British wanted to expand their trade from the seaports into the heartland of China.

The opium wars followed from 1840 to 1842. America had no diplomatic or military force in China so we let England fight the war and we moved into the heartland of China behind the British.

Although Americans offered little competition to the British, the British were vulnerable to our Yankee ingenuity. Because we had few products to trade, Americans became a mercantile force—speedy clipper ships raced across the ocean in 90 days instead of 4 months.

Americans sailed the ships more efficiently and realized greater profits than the British. We were suppliers for the British and both countries benefited from the relationship.

Americans differed from the British in other ways. In contrast to the British who sought territorial claims in Asia, Americans wanted to generate profits in China that could be transferred home.

Instead of investing in China, men like John Murray Forbes put his Asian-earned fortune into developing American railroads in our Middle West. Others turned to textiles, steamships and somewhat later, telephone and electrical equipment—providing markets for our surplus labor and production facilities—(which need exists today).

But business practices in East Asia—China, Japan, Thailand, Korea, India, Indonesia—have been difficult for Americans to readily understand.

Confucianism established rules of proper conduct for all people. So, of course, the Chinese are excellent hosts, willing to share their possessions with traders.

But they are not willing to accept the exclusivity of European or American thought and religion. They believe strongly in retaining their ethnic Chinese cultures.

For very practical purposes, the scholar-officials encouraged this behavior. In the recently published book, "Sentimental Imperialists," Professors Thomson, Stanley, and Perry say, "It is possible for a Chinese Christian convert to burn incense to his or her ancestor, offer prayer sticks at Buddhist temples, pause reverently at Taoist roadside shrines, follow the precepts of the sage Confucius—and also be a practicing member of a christian denomination.

"What seemed bafflingly characteristic was a disregard for a single deity, a zest for the here and now, and a boundless capacity to absorb credos and forms of worship. To more rigid Westerners, the combination was exasperating."

Although the Chinese were liberal in accepting differing religions, they remained adamant in their belief that China exhibited cultural superiority. The downfall of imperial, wealthy China was inevitable. China became complacent. Their historical, cultural superiority could not carry them through a new age, one of sophisticated technology.

Philosophers tell us we must study history so we are not forced to repeat it. As an amateur historian who is also a small businessman, I see parallels between world trade in the 18th and 19th centuries and world trade today.

America is similar to imperial China; international corporations mirror Britain; and small business plays the role of young America.

America today compares to imperial China. Like China, America is becoming complacent. We have laws that insist on imposing our cultural supremacy on other nations.

America even exercised the tribute system. After World War II, foreign government leaders came to Washington to acknowledge our superiority and we bestowed upon them economic aid for their countries.

Professors Thomson, Stanley, and Perry say,

Americans should keep in mind * * * diverse authoritarian patterns that underlie societies whose traditions are not the same as those of the United States—and whose histories are far longer.

Americans should also beware of reverting to their national itch to reshape the world, especially Asia, in their own image. That way lies vexation, disillusionment, and worse.

The results of the Vietnam war may have shaken some of America's sense of superiority.

To continue my comparisons, 1980 multinational corporations are like the British of the 18th and 19th centuries. They have great power, certainly not controllable by small business, and they have excellent contacts in the world of international trade.

And like the British who have been America's oldest ally, large corporations are allies of small business.

And so my third parallel. Small business in the 1980's is like America in the 18th and 19th centuries. Just like earlier American traders, small businesses are more flexible, more innovative and resourceful than large international traders.

And small business is similar to 18th and 19th century America in another way. Yankee traders brought their profits home to build America's railroads and textile industries.

Now small businesses bring our profits home to provide jobs and to utilize America's industrial facilities. We must rely, instead, on commission merchants.

Let me now bring one small businessman's history to June 1982.

As I said in the beginning of my testimony, I would like to expand my companies' international trade.

Nearly—over—80 percent of my business is with international corporations. We supply 20 percent of their orders to us overseas.

Multinational corporations appreciate my firms' flexibility and innovativeness. But they demand that we have a presence in the countries in which they are conducting business.

If we are to maintain the remaining 80 percent of their domestic—U.S.—business, which employs American workers, Shaw Mudge & Co. must operate overseas.

As I previously said, small businesses cannot afford extensive overseas offices. Small business must rely on commission merchants or become minority shareholders in foreign companies.

As a small businessman, I have no control over the activities of my customers. And I surely have no control over boards of directors of companies in foreign countries in which I have minority share.

I can make my wishes known quite forcefully regarding proper conduct, but I cannot control the actions of the local majority stockholders.

I could not pretend to guess what activities they are involved in.

But my business in the United States is unstable until I can operate confidently overseas. Providing stability overseas allows me to qualify as a supplier in our country.

Two months ago, I forwarded to your committee an amendment to the FCPA's section 104. The new paragraph deals exclusively with American firms owning minority shares in an overseas company.

This amendment has the support of NSB—National Small Business Association—and SBANE—Smaller Business Association of New England. I am a board member of both organizations.

I am honored to testify before your subcommittee today and to participate in America's Government process. This is significant to me because, as I said before, I take pride in being an American and a small businessman.

I also take pride in being an active and involved member of the Democratic Party for over 30 years. I do not want corruption in America.

I especially do not want another Watergate or tainted money from corrupt ventures to fund Presidential campaigns. There is absolutely no excuse for those activities in our country.

I am speaking to you today as a small business person supported by NSB and SBANE.

Their assure me that the business problems of Shaw Mudge & Co. are not unique. Their problems are shared by other small businesses.

Specifically, I must maintain and expand my business to protect my American business, my staff and my workers.

I also need to bring back my share of profits to America so I may continue to employ more Americans.

My question to you is this: Must I give up 80 percent of my U.S. business because I do not know exactly what my overseas customers or majority stockholder partners are doing? Many of my customers are very successful American businesses that are trading very profitably throughout the world. Can you solve my problem?

Thank you for allowing me to bring my problem to your committee today for a solution.

Mr. SWIFT [presiding]. Thank you very much, Mr. Mudge.

Mr. McGeady.

STATEMENT OF EAMONN McGEADY

Mr. McGEADY. I am Eamonn McGeady, president, Martin G. Imbach, Co. I served in the U.S. Army Corps of Engineers in Europe for a number of years. And also worked in a major local shipyard. As part of that latter duty, I dealt with many foreign nationals. That is the days when the U.S. shipyards were still competitive.

Our overview, or my overview of the Foreign Corrupt Practices Act, was brought into very close focus some years ago not too long after enactment of the act, 1979, to be exact.

Our firm was approached to build 50 anchor buoys for Nigeria, the Port of Lagos. Nigeria at that time, some of you may recall, was involved in an almost explosive expansion and goods being

shipped into the country by sea were simply languishing in the Port of Lagos.

The Government decided they needed to have some safe anchorage buoys after storms had piled a couple of ships one upon the other. They went out on the international market. They had not internal capability in this area.

Because we had done some work similar to this for some local customers, we were approached, among others. In negotiations over a couple months, we got to the point where we had acquired all of the information necessary, including, because of my earlier contacts, the ability to put a small ship, heavy-lift carrier type, charter it, put the buoys on the ship, deliver it to Nigeria and unload them in place without having to depend on any Nigerian cooperation, which at that time was notoriously poor.

We came down to a trip to New York to sign the contract and at the signing, I was advised that a commission of approximately \$75,000 would be required, and being an attorney, although not a practicing attorney, and being somewhat aware of the activities of the Congress, I decided that this was awfully close to the border with respect to the Foreign Corrupt Practices Act.

Finessed that particular meeting, came back to Baltimore, spent a rather horrendous 2 days trying to research the whole thing, at which time the Nigerians insisted we sign or back out because they had another commitment from an English-Danish consortium, and at that point, very frankly, we said it is too close to call and we backed out.

Subsequently—this is 6 or 8 months later, in discussion of this with another friend in the export-import business, she said, "I had the same problem. I had an order for 500 air-conditioners but they would only pay the draft dockside in Nigeria, not delivered in the harbor, dockside."

Well, at that time, ships were taking as much as a year and a half to get unloaded in Nigeria. Some operators were sending ships over with cement in them that they knew would be solid by the time it got unloaded and they just chartered an old rust bucket, took it over there and left a minimum crew on it and various arbitration things are going on still, as far as I know.

But in order to get these air-conditioner unloaded, there was a payment required to the port personnel, the Nigerian port personnel.

The air-conditioners had to be unloaded before the letter of credit would be honored.

So in that case, this person also backed off and said, no, no way.

I simply tell you those stories, one, a personal one and the other a personal-knowledge one, to point out the vagaries of the FCPA.

Now here I can consider myself reasonably well-educated and able to read the English language and in reading the text and trying to determine what our situation would be, I simply put myself, say, 3, 4, 5 years down the road when some eager assistant AG comes in and says, "You shouldn't have done that 4 years ago."

Now, 5 years down the road, it may be very apparent we should not have done it, but at the time, it clearly was not apparent, but it would be too close to call and we opted to back out.

I think that is the major problem with the act. The inability of a reasonable businessman who does not have larceny in his mind, who is simply trying to exercise a reasonable opportunity in a foreign market and who, particularly in the case of a small businessman or woman does not generally have the expertise that is available to larger companies.

This is another key point that I would like to make to the committee, that smaller businesses as a rule do not have the ability to staff a legal department or a foreign operations department or whatever name it would come under in order to be able to be reasonably assured that their activities meet all the terms of the law, not just the FCA, but a broad spectrum.

I invite the committee's attention to a document I am sure you have in your files somewhere, the "President's Report on the State of Small Business," transmitted to Congress in March of this year, notably page 172.

There is very succinct language in there that makes the point that I cannot make as well.

I think in general, the problem that we see, or that I see as a small businessman, interested in participating, particularly in Western Europe and in the Caribbean, is the attempt, as I see it, to impose our set of rules and regulations on foreign nationals over which we really have no control.

I agree with the principles of the Foreign Corrupt Practices Act. I do not personally believe that bribes, or other types of payments, should be required to do business. It leads to all kinds of problems that we all saw demonstrated in Lockheed and other areas that were unfortunate, both to the image and to the political realities of the United States.

But I submit to you that where commissions, for example, are a normal course of business, in some areas it is terms grease, or whatever—I don't mean grease the Nation, but the smoothing of payments, pointed out in the Chaffee bill, Senate 708.

I think most of those amendments are very appropriate. I think they should be well-recommended to your body.

We in Maryland, coincidentally enough, just last week started a self-help program to try to bring smaller businesses into the export area.

It is called MITA [Maryland International Trade Association]. It is a consortium of private-sector and governmental people. The Governor kicked it off. It will be funded initially by the private sector with technical assistance from the economic development staff of the State and the Economic Development Council of the Greater Baltimore Committee.

It brought together people who were experienced in export from the Baltimore area such as McCormack & Co. and Black & Decker, and freight forwarders and attorneys that deal in foreign commerce together with economic development people and all interested small businessmen.

Nearly 140 folks showed up. I think that points out that there is a definite interest on the part of the small business people to participate, to try to penetrate this market.

Let me make one other brief point, I think perhaps this has been overlooked, the small businessperson getting into the export

market is, generally speaking, risking a far larger portion of his or her capital than is a larger business.

The actual dollars clearly would be smaller, but in our case, where this Nigerian venture was of the nature of \$4.5 million over a period of about 18 months, would have been a lead-pipe cinch for us.

That, as a percentage, the risk involved in that, as a percentage of our total value, is quite high. Not that we are unwilling to take risks, that is what the whole entrepreneurial system is built on.

But I suggest to you that when you take that risk, and let me make clear that, generally speaking, foreign business is profitable, that is why we are there or interested in getting there, but when you take that risk, you ought to have some reasonable assurance that, one, you can get paid; and two, you are not going to be prosecuted by your own government.

When you start stacking the intangibles, the risk, possibility of not getting paid and in some instances, the clear possibility of prosecution by your own government by an ex post facto decision, then I submit that that is when the prudent businessman says, "I don't need that, or I can just not justify the risk."

I suggest that what you are considering here in your oversight hearings, the changes that you are considering would go a long way toward reducing that uncertainty.

The American businessman from the time that Shaw was speaking of, from the time of the clipper ships that sailed out of Boston and Salem and Baltimore and Philadelphia and other places, have built this country, built its strong sense of independence, those people can be re-created by the 1980's businessman but they can't do it with, figuratively speaking, both legs shackled and both arms tied behind their backs.

I have seen in my day when I lived in Europe, the American construction industry was the respected pillar in the world. We now are a poor sixth, seventh, eighth.

We are getting our heads handed to us in a basket by the Koreans, Germans, Italians, French. They are just eating us up because their governments support their companies in their export attempts.

I suggest to the Congress that you take a hard look at what we are doing in this country and try to encourage groups such as MITA, these new groups, and individual business people, to penetrate the foreign trade market for the good of this country and, of course, for the profitability of American business.

When you look at the unused industrial capacity in the Northeast and think what that could do, a billion dollars in trade is worth, by some people's calculations, 40,000 new jobs positive trade balance, I think our economic problems and our economic woes is something we cannot afford to not take advantage of.

Thank you for your time. I would be glad to respond to questions.

Mr. SWIFT. Thank you very much, Mr. McGeedy.

Mr. Featherman.

STATEMENT OF BERNARD FEATHERMAN

Mr. FEATHERMAN. Mr. Chairman, and members of the subcommittee, I am Bernard Featherman, president of Western Steel Co. of Philadelphia, Pa. I am here today to speak about some of the concerns of small business.

My company is an independent, privately owned family steel processing business, established in 1932. We sell steel products domestically and worldwide.

We export basic steel materials and finished steel products for consumer and industrial use. We represent about 175 people in sales, factory and office personnel.

I was an elected delegate to the 1980 White House Conference for Small Business and served as cochairman of International Trade for United States Region III.

Presently, I serve on the Small Business Advisory Board of the city of Philadelphia.

As a small businessman who exports and operates a DISC export trading house, I am particularly concerned with the general inequities with which Federal legislation affects small American businesses selling overseas.

Recognition of our special needs has generally not taken place. An attitude has prevailed that giant companies represent the needs of all businesses and that, somehow, what is good for big companies is good for all American businesses. This is not so.

Naturally, many measures that benefit large companies do benefit small ones, too. But many times, legislation that is advantageous to large firms places small companies at a disadvantage.

In the steel industry, the Trigger Price Mechanism (called TPM) helped large steel companies prevent import dumping by foreign steel mills, but the Government regulation contained a loophole which permitted foreign-owned steel service centers and distributors to import steel at lower prices than American-owned small and big steel service centers could compete against.

Maritime legislative reform legislation is urgently needed. Big companies have had the swat to obtain lower rates than small exporting companies.

We need to offer carriers the opportunity to pool, merger or lower rates to meet foreign competition with open conference rates and offer these lower rates to small business exporters.

When loading containers at the piers in Philadelphia, the costs run almost \$30 per metric ton.

When my company loads containers at our own warehouse with our own union labor, it costs us about \$4 per metric ton. On a 600-metric-ton shipment to the Republic of China, we saved in loading containers ourselves about \$15,000 and that got us the order.

Small business exporters like ourselves, without such facilities or loading equipment or union labor of their own to load their own orders cannot compete with such charges unless rules are changed.

Big companies have foreign-speaking personnel and in-house staff to take care of documentation work while small business exporters mainly do not.

Some financial incentives must be legislated to encourage small businesses.

Small businesses need more sophisticated financial services when exporting their goods internationally than they presently receive from their bankers for their domestic sales.

Many foreign competing exporters are subsidized with lower interest rates to help finance their international sales.

To encourage companies to export, foreign exporters also enjoy greater borrowing capacities on lines of credit extending to as great as a 20-to-1 ratio—loan amounts in proportion to net worth of company.

American companies, both large and small, with domestic sales only, could probably receive up to a 2-to-1 ratio.

Those small companies exporting probably only receive a 1-to-1 ratio, in many cases. Small businesses, for the most part, are at a competitive disadvantage.

On financial leveraging, legislation is needed to change this ratio to encourage more exporting.

In my travels overseas, I have noted that many foreign export trading houses have banks participating in an equity investment position on their boards.

Banks serve both as minority stockholders and as management participants. This gives foreign exporters an extra edge to obtain necessary capital when needed for joint ventures, setting up factories to make products for export, lines of credit for purchasing materials, financing sales by sellers and by overseas purchases.

I support banks participating in an equity position in export trading companies, yet I do so with considerable reservations.

We must be sure to provide built-in legislative safeguards to protect the integrity and soundness of the bank itself, and to protect both small businesses and the public sector.

We must maintain a constant vigil to assure against antitrust concerns detrimental to small business participants. We must guard against banks partnering largely with large businesses and freezing small businesses out.

Since most banks are big businesses and getting larger, risk of giant trading house-bank combines shutting out small business from export trade is substantial.

Incentives should exist to encourage bank alliances with small firms. Bank participation on export trading companies must be held to a maximum of 20 percent equity ownership or perhaps to hold the banks' investment to a maximum of 5 percent of its consolidated capital and surplus.

Legislation should be instituted so banks would be encouraged to loan on a two-tier interest rate system, with lower rates given to small business exporters.

Perhaps a difference in the prime rate less 25 percent discount or a similar reduced rate, with tax credits or Government subsidy would be a good incentive for both the banker and the small exporter to be offered.

This subcommittee should consider the possibility of removing the antitrust implications of the present Webb-Pomerene Act. We need small and large businesses in specific industries to join together in cooperative ventures to sell their goods overseas.

Under one banner, a specific industry could export cooperatively and successfully. Our company was approached not too long ago by

a big business competitor to explore a Webb-Pomerene association, but probably because of the antitrust concerns, the vagueness of the act's language and possible hostility by the Justice Department, nothing was done about it.

I am sure we could start again to consider such an export vehicle if favorable legislation is enacted in the future to grant antitrust immunity certifications to the participants.

Many American exporters face the problems of adhering to restrictive Government regulations, whereas foreign export companies engage in the very acts declared illegal by our country.

In some countries, doing business is risky because of the corruption. Frankly, I have not been asked by any of my customers abroad for what I consider payoffs.

That may be because I deal largely with small- and medium-sized companies and deal directly with the owners who are interested only in the best price.

However, many of my business colleagues and friends who export tell me they have problems over demands for tips or payoffs.

Some agents overseas request additional commissions or payments far in excess of standard agent commission rates for specific orders.

They claim payments must be made to third parties to secure those orders by so-called gross payments or overcharges.

Some foreign buyers want to be overcharged and the excess amount put in a U.S. bank in their name because they cannot take money out of their own country.

Many foreign competitors engage in these practices, resulting in taking away orders from American firms.

An example of corruption in one of the African countries is the practice of paying illegal cash payments to a government official who controls the release of dock receipts which customers need to pick up merchandise from the piers.

Unless this illegal payment is made, merchandise could possibly stay on the docks for up to a year or more after arrival in that country.

That was addressed by the former speaker.

Another example of illegal payments are those made beyond normal commissions to a foreign agent or representative to allegedly take care of the person responsible for approving or authorizing the purchase.

We have heard of many stories where American companies that export have to do it and of foreign companies who engage in these questionable payments also, in order to secure business overseas.

I am sure both big and small American businesses have lost substantial orders because of our restrictive legislation while foreign governments look the other way or encourage it tacitly when their country's exporters "buy" business through these types of unethical, unfair arrangements.

Our laws should be modified to permit American exporters to be at least competitive against practices engaged in by foreign competitors in foreign countries.

While we need changes in legislation for exporters, here is an example why we also need legislation changes for domestic companies fighting unfair, subsidized imported products.

Both small and big businesses stand together against a questionable practice currently going on in the steel industry. It is called triple distribution and is engaged in by foreign steel mills.

Foreign steel producers have entered the American steel distribution industry by owning chains of steel service centers, which sell against domestic-owned steel service centers in our country.

Sales are suspect as to legality as made by foreign-owned centers. Many prices for steel already fabricated are below, at cost, or slightly above the actual cost of the basic steel materials bought by domestic-owned small and big service centers.

The question is, How can a company sell without covering its overhead costs?

Perhaps by illegal allowances given by foreign-owned firms, questionable claims to affect lower pricing, perhaps by dating terms extended sometimes up to a year longer, which, in effect, is an illegal pricing discount.

Perhaps by discounts on material directly or selling prime materials as seconds, so a lower price is given, or even by varying extras, thereby reducing prices, which domestic-owned companies could not obtain from their steel sources.

To compound these unfair practices, foreign steel producers recently put in-field depot warehouses that store from 1,000 up to 100,000 tons of steel at specific locations nationwide.

The steel is sold at heavily discounted prices which are considerably below American steel producer prices, resulting in the long-range implications of putting domestic steel companies, big and small, out of business in the future.

This is happening now. We all know the scenario to follow—cartels, price-fixing, and consumer price increases—all illegal, all unfair, all very possible.

Yet, American companies could not do this overseas due to foreign countries whose governments have restrictive, protectionistic practices to cover their home steel industries.

I would like to touch on a list of areas where small companies are disadvantaged in this area.

One, foreign market knowledge; two, financing; three, credit risk-taking; four, representation in foreign countries; and five, regulations.

What we need really is to establish a one-stop export center on a localized basis in each section of the country.

Analyze markets for market opportunities, including import-export trends of foreign businesses to uncover untapped markets.

Establish a network of American multinational companies to help "piggy back" exports overseas on an international supplier base for America's small businesses.

Target industries that can be coordinated with present export companies and future business exporting companies.

Encourage investment incentive strategies for small businesses that want to export.

As small businessmen, we are survivors—good street fighters—resilient. We must innovate to export. We must be willing to take risks to export. Business must export, for those that do not grow and change, almost invariably are eliminated.

A new era is ahead with virtually unlimited opportunity. I hope you can help us.

Thank you.

[Mr. Featherman's prepared statement follows:]

FOR: U.S. House of Representatives
Committee on Energy and Commerce
Subcommittee on Telecom Consumer
Protection & Finance
Rayburn House Office Bldg.
Washington, D.C.

FROM: Western Steel Company
4424 Paul St.
Philadelphia, PA 19124
215-744-9300

DATE: 9:30 AM June 8, 1982

Mr. Chairman and Members of the Sub. Committee:

I am Bernard Featherman, president of Western Steel Company of Philadelphia, Pennsylvania. I am here today to speak about some of the concerns of small business. My company is an independent, privately owned family steel processing business, established in 1932. We sell steel products domestically and world-wide. We export basic steel materials and finished steel products for consumer and industrial use. We represent about 175 people in sales, factory and office personnel.

I was an elected delegate to the 1980 White House Conference for Small Business and served as co-chairman of International Trade for U.S. Region III. Presently, I serve on the Small Business Advisory Board of The City of Philadelphia.

As a small businessman who exports and operates a DISC export trading house, I am particularly concerned with the general inequities with which federal legislation affects small American businesses selling overseas. Recognition of our special needs has generally not taken place. An attitude has prevailed that giant companies represent the needs of all businesses and that, somehow, what is good for big companies is good for all American businesses. This is not so.

Naturally many measures that benefit large companies do benefit small ones, too. But many times legislation that is advantageous to large firms places small companies at a disadvantage.

In the steel industry, the Trigger Price Mechanism (called TPM) helped large steel companies prevent import dumping by foreign steel mills but the government regulation contained a loophole which permitted foreign owned steel service centers and distributors to import steel at lower prices than American owned small and big steel service centers could compete against.

Maritime legislative reform legislation is urgently needed. Big companies have had the swat to obtain lower rates than small exporting companies. We need to offer carriers the opportunity to pool, merger or lower rates to meet foreign competition with open conference rates and offer these lower rates to small business exporters. When loading containers at the piers in Philadelphia, the costs run almost \$30 per metric ton.

When my company loads containers at our own warehouse with our own union labor, it costs us about \$4 per metric ton. On a 600 metric ton shipment to the Republic of China, we saved in loading containers ourselves about \$15,000 and that got us the order. Small business exporters like ourselves without such facilities or loading equipment or union labor of their own to load their own orders cannot compete with such charges unless rules are changed.

Big companies have foreign speaking personnel and in house staff to take care of documentation work while small business exporters mainly do not. Some financial incentives must be legislated to encourage small businesses.

Small businesses need more sophisticated financial services when exporting their goods internationally than they presently receive from their bankers for their domestic sales. Many foreign competing exporters are subsidized with lower interest rates to help finance their international sales. To encourage companies to export, foreign exporters also enjoy greater borrowing capacities on lines of credit extending to as great as a 20 to 1 ratio (loan amounts in proportion to net worth of company). American companies, both large and small, with domestic sales only could probably receive up to a 2 to 1 loan ratios. Those small companies exporting, probably only receive a 1 to 1 ratio, in many cases. Small businesses, for the most part, are at a competitive disadvantage. On financial leveraging legislation is needed to change this ratio to encourage more exporting.

In our own company's situation, one potential joint venture with a company from a French speaking African nation was successful because the \$100,000 sale of machinery was too small to be put through the Export-Import Bank and our local banks felt the sale too risky, even though we had almost \$50,000 net profit in the deal.

In my travels overseas, I have noted that many foreign Export Trading Houses have banks participating in an equity investment position on their boards. Banks serve both as minority stockholders and as management participants. This gives foreign exporters an extra edge to obtain necessary capital when needed for joint ventures, setting up factories to make products for export, lines of credit for purchasing materials, goods-in-process or finished inventories and financing sales by sellers and by overseas purchasers. Foreign banks involved with export trading companies undoubtedly have branches in not only our country but throughout the world to assist in export opportunities and marketing information. They find overseas trading partners, supply special services in financing, provide financial leverage and lines of credit, as well as leverage in foreign exchange transactions.

I support banks participating in an equity position in export trading companies, yet I do so with considerable reservations. We must be sure to provide built in legislative safeguards to protect the integrity and soundness of the bank itself, and to protect both small businesses

and the public sector. We must maintain a constant vigil to assure against anti-trust concerns detrimental to small business participants. We must guard against banks partnering largely with large businesses and freezing small businesses out. Since most banks are big business and getting larger, risk of giant trading house-bank combines shutting out small business from export trade is substantial. Incentives would have to exist to encourage bank alliances with small firms. Bank participation on export trading companies must be held to a maximum of 20% equity ownership or perhaps to hold the banks' investment to a maximum of 5% of its consolidated capital and surplus. Legislation should be instituted so banks would be encouraged to loan on a two tier interest ratesystem, with lower rates given to small business exporters. Perhaps a difference in the prime rate less 25% discount or a similiar reduced rate, with tax credits or government subsidy would be a good incentive for both the banker and the small exporter.

This sub committee should consider the possibility of removing the anti-trust implications of the present Webb-Pomerene Act. We need small and large businesses in specific industries to join together in cooperative ventures to sell their goods overseas. Small businesses are diverse and complex. Galvanized together, small and large businesses can open new markets internationally by selling in very competitive pricing ranges and in large varieties and quantities overseas. Under one banner, a specific industry could export cooperatively and successful. Our company was approached not too long ago by a big business competitor to explore a Webb-Pomerene Association but probably because of the anti-trust concerns, the vagueness of the acts' language and possible hostility by the Justice Department, nothing was done about it. I am sure we could start again to consider such an export vehicle if favorable legislation is enacted in the future to grant anti-trust immunity certifications to the participants.

We can't ignore what foreign competitors are doing in the export market. In the reality of doing business overseas, many American exporters face the problems of adhering to restrictive government regulations, where as foreign export companies engage in the very acts declared illegal by our country. In some countries doing business is risky because of the corruption. Frankly, I have not been asked by any of my customers abroad for what I consider payoffs. That may be because I deal largely with small and medium sized companies and deal directly with the owners who are interested only in the best price. However, many of my business colleagues and friends who export tell me they have problems over demands for tips or payoffs.

Some agents overseas request additional commissions or payments far in excess of standard agent commission rates for specific orders. They claim payments must be made to third parties to secure those orders. Most businesses frown upon this practice and lose the business rather than engage in illegal undertakings contra to our laws pertaining to so-called grease payments or payoffs. Some foreign buyers want to be overcharged and the excess amount put in a U.S.A. Bank in their name because they cannot take money out of their own country.

Many foreign competitors engage in these practices, resulting in taking away orders from American firms. This may, more than may not, be fact in most cases; however, with restrictions placed on American exporters, foreign companies will continue to "buy" overseas orders in many forms.

An example of corruption in one of the African countries is the practice of paying illegal cash payments to a government official who controls the release of dock receipts which customers need to pick up merchandise from the piers. Unless this illegal payment is made, merchandise could possibly stay on the docks for up to a year or more after arrival in that country. In many instances, the exporter of record could not get his money from the banks because a signed, receipted dock release was needed for release of payment. If the importer could not get the material released, he suffers lost sales and the exporter would not have the use of his capital or profits on the sale.

Another example of illegal payments are those made beyond normal commissions to a foreign agent or representative to allegedly take care of the person responsible for approving or authorizing the purchase. We have heard of many stories where American companies that export have to do it and of foreign companies who engage in these questionable payments also, in order to secure business overseas. I am sure both big and small American businesses have lost substantial orders because of our restrictive legislation while foreign governments look the other way or encourage it tacitly when their country's exporters "buy" business through these types of unethical, unfair arrangements. Our laws should be modified to permit American exporters to be at least competitive against practices engaged in by foreign competitors in foreign countries.

While we need changes in legislation for exporters, here is an example why we also need legislation changes for domestic companies fighting unfair, subsidized imported products. Both small and big businesses stand together against a questionable practice currently going on in the steel industry. It is called Triple Distribution and is engaged in by foreign steel mills. Foreign steel producers have entered the American steel distribution industry by owning chains of steel service centers, which sell against domestic owned steel service centers in our country. The only thing is, those sales are suspect as to legality, as made by the foreign owned steel service centers. Many sale prices for their steel already fabricated were below, at cost or slight above the actual cost of the basic steel materials sold by domestic owned small and big steel service centers. The question is how can a company sell without covering its overhead costs? We can cite illegal allowances given by foreign owned firms which were made for questionable claims to effect lower pricing, dating terms extended sometimes to a year or longer which in effect is an illegal pricing discount, discounts on materials, selling prime materials as "seconds" so a lower price is given, or waiving of extras thereby reducing prices which domestic owned companies could not obtain from their steel sources; and to compound these unfair practices, foreign steel producers recently put in Field Depots which are warehouses that store from a thousand tons of steel up to as much as 100,000 tons of steel at specific locations nationwide. The steel is sold at heavily discounted prices, which are considerably

below American steel producer prices, resulting in the long range implications of putting domestic steel companies, big and small, out of business in the future. This is happening now. We all know the scenario to follow - Cartels, price fixing and consumer price increases - all illegal, all unfair, all very possible. Yet, American companies could not do this overseas due to foreign countries whose governments have restrictive, protectionistic practices to cover their home steel industries.

Having covered a variety of issues involving exporting, I would now like to list areas in which small businesses are disadvantaged when trying to enter international markets and could use government help.

1. FOREIGN MARKET KNOWLEDGE: Such as which countries to sell to, customs, political risks, who to sell, how to communicate. the Department of Commerce makes some help available, but more is needed.
2. FINANCING: Where can the small business get adequate working capital to cover materials, labor, delays in shipping and receiving payments, documentation and how to collect our monies.
3. CREDIT RISK TAKING: Foreign risks are tougher than domestic sales. Currency rate exchange fluctuations vary from country to country. Rate insurances are needed for small businesses. Political situations affect credit situations in various countries.
4. REPRESENTATION IN FOREIGN COUNTRIES: Who are the distributors, agents or customers? Where can we get the help for assistance to overcome language problems, servicing what is sold, travel cost subsidies and proper freight forwarders.
5. REGULATIONS: Tariffs, duties, licensing information needed on products and countries sold. Metric systems, Packaging requirements. Documentation knowledge.

and we need to:

- a) Establish a one-stop Export center on a localized basis, in each section of the country.
- b) Analyse markets for market opportunities, including import/export trends of foreign businesses to uncover untapped markets.
- c) Establish a network of American multi-national companies to help "piggy back" exports overseas on an international supplier base for America's small businesses.
- d) Target industries that can be coordinated with present export companies and future business exporting companies.
- e) Encourage investment incentive strategies for small businesses that want to export.

Small businesses are the backbone of the American economy. Small businessmen swell the ranks of supporters for our economic system. The small businessmen of this country, with their families, represent a substantial block of citizens, without whose support big business might find itself relatively isolated from mainstream sentiments and concerns. It is small business, not big business, whom voters identify with when they cast their votes for policies or candidates favorable to business concerns. Most Americans own or have some family owning some type of small business.

Americans have always been a nation of "can do" and that is the name of the export game. But we must make a total commitment to export. We must get to know about our foreign neighbors, learn their languages and customers. Understand their economies. And buying habits.

We can get a great deal of information to help us export and some of it is available but needs better coordination. Through our chambers of Commerces, Industry and trade associations, World Trade Clubs, private export consultants, export management companies and banks. The most important source of aid, The United States Department of Commerce, has been very cooperative and extremely helpful with all kinds of information. Even our state and city Department of Commerces are excellent resources for data.

As small businessmen, we are survivors - good street fighters - resilient. We must innovate to export. We must be willing to take risks to export. Business must export, for those that do not grow and change, almost invariably are eliminated. A new era is ahead with virtually unlimited opportunity. I hope you can help us..

Mr. SWIFT. Thank you very much, Mr. Featherman.

We are trying to work our way through a process here in which we get a better understanding whether it is the law that needs to be changed, or if it needs to be clarified in some official way so it can be better understood and implemented.

Mr. McGeady, I understand you are an attorney. Perhaps you could help me.

Relative to the specific kind of thing you were talking about, for example, the people holding things up on the docks or not letting them dock: The laws says that the term "foreign official" does not include those government employees whose duties are essentially ministerial or clerical.

That would seem at first blush to apply to the people that needed greasing in the specific instance you mentioned.

Obviously in your case and in the case of the exporter of air-conditioners, your firms did not feel, apparently, that this was sufficiently clear.

Would you expand why you were unwilling to go ahead with the deal on the basis of the language that I just read?

Mr. McGEADY. Mr. Swift, let me make two quick points, one, the mooring buoy deal I have close personal knowledge of, the air conditioner deal would come under the heading of hearsay.

But speaking to the question of essentially ministerial or clerical, the problem there is, as we see it, or as I see it, I should say, is that it is not clear what ministerial or clerical means in 1982, compared to what it might mean 4 years from now when somebody finally is, 3, 4, whatever timeframe we are talking about now, before somebody in either Justice, or Commerce or whoever, would say, "That was a no-no. You should not have dealt, Mr. McGeady, with the port director at Lagos because his job was clearly not ministerial or clerical."

I would say, yes, it was.

Then you get into an argument as to whether it was or not.

Mr. SWIFT. Do I understand you to be saying that you don't want to be second-guessed 4 years later by a bright young law school graduate who was an undergraduate when you made the decision.

Mr. McGEADY. Essentially that is correct. Going further to the mooring buoy deal, the person we were dealing with in New York was a Nigerian national; our bank, which had a strong international department, both on the African Continent and in London, had checked out, as best they could, as prudent business people, the creditworthiness, the ability of the person to award the contract, the fact he was who he said he was, and we had to determine that he was, indeed, not a government official, not employed by the government.

He was, in fact, a procurer. He had a whole series of contracts, construction-type contracts that he was going to various communities and getting bids on.

We did lose that job to the British-Danish consortium for about \$1.25 million higher than our price. Their price was higher.

We are going to use a better mousetrap. We had the buoys that are built by a Virginia firm that are used all over the world in off-shore drilling and things like that.

We just adapted their use to the Nigerian requirement and they were tickled. They didn't require maintenance, they served all the purposes they wanted, and so on.

But the commission payment, which was of the nature of 2½ percent of the contract, was well within what anybody would consider commission terms just made us back off.

It was not a good judgment call. Strike that. I think it was a good judgment call on our part, it was too close to call.

Mr. SWIFT. It was not easy to make a judgment call?

Mr. McGEADY. Right, and given other intangibles, the only prudent thing to do is back off.

Mr. SWIFT. Let me ask you this because you are a small business panel, do you think that had you been a large business with greater resources for legal research and so forth, that you might have been able to narrow that down so that the call would have been any easier or do you think in this particular instance it really had little to do with whether you were a small business or not?

Mr. McGEADY. I think the former is clearly the case. I subsequently found out that you can go to Justice and/or Commerce and get what amounts to an opinion as to whether what you have proposed to do is falling within or without the purview of the statute.

That was much later. That was well after the opportunity was gone.

If we had been a larger business and if I had had resources to get one of the many excellent law firms in Baltimore to do 10,000 or 15,000 dollars' worth of research for me, the chances are I would have gotten an answer that would have allowed me to call it probably in our favor.

Subsequently, I think that we could have proceeded with not substantial risk.

I am talking legal risk. I am not commenting on the business risk.

Mr. SWIFT. One of the dilemmas we are dealing with is that there are different points of view on the committee.

One of the prominent points of view is that we really don't want to make drastic changes in this law which would be interpreted, reasonably, by American businessmen or foreign businessmen and interests as saying we are giving a green light to corrupt practices.

Therefore, that particular point of view is looking for some way other than major amendment to the law to try to clarify these things.

Another point of view is just go ahead and do what the Senate did and clear it up that way.

Going back to the first point of view, do you think there are things within the confines of the present law that could be done administratively to help ease the situation? Let me suggest two possibilities and I would appreciate anybody on the panel commenting on whether you think they are practical.

One would be to have clearer definitions made by administrative agencies.

Second, to have a greater outreach, particularly to small business by the relevant departments and agencies so that the small businessman doesn't find himself in the position of finding out 18

months later that he could have had this expertise made available to him.

Would those two approaches be a significant help to small business or do you think that that is just playing around with a bad situation and it is better to correct the law itself?

Mr. McGEADY. If I may respond initially. Two things come to mind. One, I believe something like that would be a definite advantage to those small businesses who choose to or are enticed into the export market.

I believe that either self-help, perhaps along the lines we have just begun in Maryland, or Commerce help. There are presently some Commerce functions in place that I am aware of.

I must admit they are awfully hard to find when you need them but I believe that at least the authorization is there.

The other thing that occurs to me is that, bear with me about the apocryphal story about Abe Lincoln where one hot July day from his second floor office, some standersby heard a loud crash and bang and this body comes tumbling out the door, followed by Lincoln in his stovepipe hat. The passerby said, Mr. Lincoln, what was the trouble? He said, that man tried to bribe me. He said, that is wonderful, you threw him out. I think that shows remarkable moral character.

And Abe said, no, he was just getting too close to my price.

My point is that perhaps Congress in its wisdom could either instruct—I don't know exactly how that would occur, but instruct Commerce to set rules. After all, in many instances commissions are paid in the United States to obtain business, perfectly normal business practice. Yet, that same commission paid to a foreign official unless that official is clearly, clearly ministerial or clerical—and I suggest to you, Mr. Swift, if you came up to a Customs officer, is he ministerial or clerical? I don't know. I really don't know.

That is not a loaded question.

A stevedore boss, whatever, keeping in mind that in many foreign countries the government runs those functions, of course. All right?

Congress perhaps could have Commerce draw up rules and regulations under which we could operate which would have clear delineations. That is a lot easier said than done, I admit, but that certainly would give us some better guidance than what we presently have.

Mr. SWIFT. Yes, Mr. Mudge.

Mr. MUDGE. I don't share Eamonn's view on the matter of regulations. I think we have to cut back on regulations. I think Congress has to bite the bullet, recognize it made a colossal mistake that many of the studies have shown probably cost this country \$3 to \$4 billion a year in lost trade. Nobody here has—because the testimony is fully in the record on support of S. 708.

I urge full acceptance unchanged S. 708 as passed by the Senate.

I don't believe that Congress will ever get around to it, I don't believe that a guy out of Harvard will get to it and I can't wait 30, 60, or 80 days for an opinion.

I cited a case last year in front of the Senate. I thought I wouldn't duplicate it but it might be useful.

My son speaks Chinese and Portuguese, I sent him to East Asia to start looking around to get agents for us. He went to an East Asian country and the man said, well, we would be interested in doing business with you, it is a soap business that is now quasi-public-private. It is half owned by the state, half by its former owners.

They gave us a project to duplicate, we put it through our machines, did a decent job because the machines show the chemistry of the product and not just the empiricism that went into it, the empirical procedures when first invented and developed 30 years ago.

So we put the latest technology in, it is less irritating and it is updated.

When he went back a second time they were pleasant, they said the inventory was still high. Two years went by, nobody has a 2-year inventory, so I sent an experienced international man out, we put about \$100,000 or \$125,000 in pursuit of this business, and also our price was about 4 or 5 percent less than we understood the competition to be.

The instruments give you a good idea of the price, they can tell you within a penny what it is.

So he took him aside in a hotel room without our local agent there. He doesn't want the local agent blackmailing him in his country.

"Look, we don't want you to drop the price, we want you to raise it 25 percent and put it in this third country bank."

I never knew of the Foreign Corrupt Practices Act. I said, let's investigate. I say I have my cause. This is a ridiculous bill. This bill was written between Thanksgiving and Christmas and you try to find anybody in this business in Washington working seriously between Thanksgiving and Christmas.

Look back this last Christmas season of 3 weeks, what happened? Nobody was in. I couldn't get anybody on the phone. They ran it through inadequate hearings in 1977.

Some day, and this is the day, somebody will stand up on the floor of this Congress and say, "Lockheed, you had guts. Somebody from Watts, who is on relief today, who may have been a junior draftsman, may have been a janitor, thank God, whoever you are at Lockheed for taking that chance in Japan. I owe my mortgage to you."

You know just as well with the State you are from that you have to compete against airplanes from the European area. I mean, we know we are talking about a lot. This cost billions of dollars of work in the United States and it must go; the Senate version I urge adoption of without qualification.

No person in the Commerce Department out of Harvard or Yale will be able to tell me in the time I have to move, like 24 hours, not 2 years, whether that company in the Third World is a private company or public company.

By the time Sherman and Sterling, Casey, Lane & Middendorf get through with it, the customer is retired. It will not work. We cannot go to larger bodies to solve it.

In this book it is adequately documented. When Perry went into Japan, who opened that up? He gave them a locomotive and 350

feet of track and a passenger car. You couldn't get into Japan doing that today because of the FCPA.

Mr. SWIFT. Where did the 350 feet of track go?

Mr. MUDGE. It is unbelievable. It is in here.

Mr. SWIFT. Did you have any comments?

Mr. FEATHERMAN. I have mixed feelings about this because I agree with both of the gentlemen.

I believe we should clarify our language so that businessmen like ourselves know where we stand and can make decisions without being in jeopardy.

I think most businessmen are honorable and honest. In fact, I say 99 percent of them.

I feel that it is very important that they know the proper interpretation of the law. So a clear definition is needed.

In like manner I have to look at it in a self-serving interest, how can we get more business for our American exporters if we have to compete against such types of competition overseas where our competition from foreign countries are doing the very thing that our Government does not want us to do?

It truly is a dilemma. I guess we have to look at it in a practical way, what is doable and what can help us get business while still staying within the letter of the law.

Mr. McGEADY. If I may, I want to make the point, Mr. Swift, despite my colleagues' protestations, I do support S. 708, the Senate bill provisions, entirely.

I still think that even with those corrections there needs to be work done with respect to the actual day-to-day operation or interpretation of the law.

Mr. SWIFT. That was my interpretation of what you said.

Before recognizing my colleague from Virginia, I would just like to put in a defense of the Congress, I was not here, but I am informed it took two sessions, it was not done between Thanksgiving and Christmas.

I recognize the gentleman from Virginia.

Mr. BLILEY. Thank you.

Mr. McGeady, I am sorry you and the Virginia firm didn't get the business.

Mr. McGEADY. We were, too, Mr. Bliley.

Mr. BLILEY. I appreciate your testimony. How would you go about it if you were sitting here as a Congressman to modify the statute in order to facilitate the type of situation you were in? That is, the ministerial or clerical business.

How would you change the law to cover the dock official that you were forced to deal with if you had decided to go forward with the price?

Mr. McGEADY. I think we need to look more carefully at—first, let me rephrase that.

First, I say again, the Senate bill 708 provisions are a good start.

Further, I think the Congress needs to look at the language and it must balance between what it perceives as the Nation's best interests that were in its perception damaged as a result of certain activities in the early seventies which resulted in this bill.

The Congress must recognize that business practices, normal business practices in other countries are not necessarily exactly as they are in this country.

We have lived under the so-called Cohan rule, ordinary and reasonable expenses rule here in the United States. Perhaps there is an avenue there where ordinary and reasonable expenses are allowed.

Now, you say isn't it hard to define that and I say to you that every businessman knows what is ordinary and reasonable and he knows that if an expense isn't ordinary and reasonable he better daggone well be ready to justify it.

I do not agree, however, and I do not believe the prohibition against heavy duty slush funds and things like that should be maintained. That is my personal opinion.

I don't think whether it is the Martin Imbach Co. or foreign nationals, that there ought to be subrosa funds that can be used for all kinds of activities.

That particular prohibition I would agree with.

But the dock official in Nigeria, for example, to pay for customs, stevedores, paper clearances, so on, in the port in question, then that ought to be allowed if you have to pay that. That is an ordinary and reasonable business expense.

Mr. BLILEY. Would the other gentleman agree with that?

Mr. MUDGE. The British have a thought that might be well to pursue. I understand any export transaction is reported in its fullest detail to the Bank of England. They have a very interesting collection of data then.

They know what makes the world go round. They don't have to rely on M15 or M16. They know what makes the world go around, whether it is selling airplane engines, mooring buoys, soap, anything else. They never prosecute, of course.

Now, look at the case of the Davy, Enserch matter, it was reported 55,000 man-years of work were lost to Enserch because the British Monopolies and Mergers Commission forbade Davy Corp., Ltd., in Scotland from merging with the Texas Enserch Corp. in September 1981; 55,000 man-years of work were lost. That is enough right there to stagger you in lost American jobs, because of the adverse effect on Davy of the FCPA.

Mr. BLILEY. Indeed, it is.

Mr. FEATHERMAN. As small businessmen our situation may be different than big businesses. You have heard about airplane situations to get orders. Of course, as a small businessman one day I would like to be a big businessman, too.

But we do face a problem of what is acceptable in the countries that we deal with and then should we deal in that country?

I think a sensitive point was taken in what is the customs of a country and what is acceptable as ordinary and reasonable to do? I have to agree with that tact. I think that we have to make it easier for people to export but, again, we do face a problem that if there are substantials going to be taken against small business people, that the small business people will not take the risk.

So I have to agree that whatever is customs in a country we should acclimate ourselves to within the letter of the law, not to do anything illegal.

Mr. BLILEY. Mr. Featherman, you cited as an example of an illegal payment, one beyond the normal commission. How do you make a determination of what a normal commission is?

Mr. FEATHERMAN. That is a very difficult question. I will try to answer it as straightforward as I can. In the United States when we sell domestically we work several ways. We work at commissions of several percentage points on the net sales or we work it where we sell a customer and then they in turn sell their customer making the difference between our price and the price that they buy it for and what they sell it for.

A good example, if they buy an item for a dollar, they turn around and make the normal 25 percent markup. We sometimes will carry the paper and bill that customer's customer direct and rebate the difference to our agent or dealer.

When you are dealing overseas it may approximate a similar situation where the agent wants you to bill the customer rather than carry the customer himself and rebate a difference to him that is not normally an agent's commission of 2 or 3 percent.

He may want to have a 25-percent gross profit.

Now, this is where we are skirting the law and it is in serious question because if it is different than the normal procedures of how you sell through that channel of distribution then you are in violation of the law according to the FCPA.

Now, I think it would have to be a question of many times small business people are at risk when they do something out of the ordinary without the knowledge but if they do it and it is illegal with or without prior knowledge they are guilty of the act.

Mr. BLILEY. Mr. Featherman, if I can follow up on that, if we were to amend the statute to say that you are able to do what is normal practice in the country and you are able to show that the resale-type transaction or the transaction where you bill the customer directly and rebate to the agent, is it normal practice for, in your case, steel sales in X country, do you think that would take care of the problem?

Mr. FEATHERMAN. We would still be on a borderline situation and I have deep concern for the small businessperson who interprets it incorrectly or has it interpreted on him.

Mr. BLILEY. How would you suggest we get around that?

Mr. FEATHERMAN. I am sorry you said that.

I am glad, however, that you are attacking the problem as you are because really that is the thing that you have to go by on an industry-by-industry basis.

What is prevalent in an industry trade has to follow through throughout the world as well.

If people are selling, and I know many times we sell overseas and we have a commission between 2 to 3 percent on the net sales in steel, we would not have the same commission on a sale of a consumer item like a metal bed, or, and we sold steel to the Far East and cots to the South American countries. One would receive a lesser commission.

In making that arrangement with an agent it is a lot different than when you make the arrangements selling to a government. It is a different situation completely. We have to comply with the letter of the law.

But if it is a private sale we question whether it is extraordinary to the normal procedures we do in business every day on an export basis.

Mr. BLILEY. Since you are all three representing small businessmen here before us, and though I wasn't here, I believe that the intent of this act was principally against large sales brought about by events that were large sales.

Would putting a dollar limit be a possibility? I have not done any research on it, I just throw this out. Put a dollar limit that sales below a certain figure would be exempt?

Mr. FEATHERMAN. I don't think you can put a dollar limit on sales on an export basis. I think you have to have a category of a type of sale. If it is a raw material and the general trade procedures are to sell at a few percentage points as a commission, then I think that that should prevail on all sales made in that specific trade.

If, however, it is a sale of a finished good where normally they have 10-percent commission, then it is reasonable that those commission people get a 10-percent commission.

Mr. BLILEY. Yes.

Mr. MUDGE. If I could, I would like to put in the record this May 24 issue of the Financial Times from London. It is read by most people who trade regularly around the world. There is an article, "The Key to Success in Joint Ventures." It has to do with India. It is touching on the question that you raise. I would just read three paragraphs from it.

Indians like to do business on the basis of friendship and Dr. Krueger thinks it is important to get to know your partners on these terms. Never, never get involved in the Indian way of doing business which is the euphemism of people offering advice to the need to pay speed money, to hasten or insure the possible outcome of bureaucratic dealings.

The term reputable covers partners who do resort to "the Indian way," when they feel it is necessary.

Agent's fees can be pretty hefty and cover a lot. We don't ask questions, a British trade official said.

We leave it to our Indian partners to fix things and then look after it later in the contract.

A Japanese trading company official said that.

There are sultans in parts of Southeast Asia where they are largely authoritarian governments that are referred to as Mr. 50-50. We are talking projects that run up into the hundreds of millions of dollars.

There is an employee of a state-owned oil company in Southeast Asia who made \$11,000 a year. His widow is suing the government for \$35 million and his bank account.

That is what we are up against, except for the last 300 years. For 2,000 years, Asia was the center of the world's culture. That is something to ponder in the long text of this instead of looking for short-term answers.

It is a cultural matter. It was what I had hoped to be able to set the mood for, the cultural differences. It really is a cultural difference.

Mr. BLILEY. Thank you, Mr. Chairman.

Mr. WIRTH. Thank you, Mr. Bliley.

Therefore, if you were sitting where we are, clearly nobody wants to see, Mr. Mudge, the United States responsible for bringing down a government in Japan, Italy, or whatever, right?

Mr. MUDGE. Well, Mr. Tanaka in Japan even in jail was the most powerful man in Japan. He is the most powerful man in Japan today.

Another matter about Tanaka, he was not put in jail for violation of laws, he was put in jail for perjury in his testimony in front of the Diet and none of those three men who worked for the private airline who have been since fined have—they still have their positions in the company, I forget the name of the Japanese airplane company.

They came under the bill there because they landed at Government facilities, the airports were Government. It is very complex.

Mr. WIRTH. I understand that but I am going back to ask you to put yourself where we are sitting. Here we have a statute enacted in 1977. It was after a whole series of events which were in some people's opinion unfortunate and in other people's opinion were criminal.

Where would you go from here? I would ask all three of you. What would you do in this situation?

Mr. MUDGE. I would move passage of 708 without change; then, that other matter about the prevention of future Watergates. I suggested language that might come in another bill at another time. I am sensitive about that and the committee staff has that material. I am told by others this is not the right place for that.

That might solve the problem that we have for slush funds coming in dominating American elections.

Mr. WIRTH. You are satisfied that the ambiguities in existing law are taken care of in the Senate language?

Mr. MUDGE. Yes, sir.

Mr. WIRTH. Mr. McGeady?

Mr. MCGEADY. Mr. Chairman, I would agree with Shaw that the provisions of Senate 708 should be carried forward.

In addition to that I would like to see further simplifications perhaps along some of the avenues Mr. Bliley has begun to explore and that is that with respect to the size of a transaction it would seem to me that the danger to the common good of the United States is not very well defined on the occasion of multiple smaller transactions.

But with regard to the bill as has been pointed out was enacted as a result of two or three fairly well publicized, generally speaking, fairly high-dollar-type transactions and that perhaps in retrospect it has been a little overkill, that the U.S. policy of not having domestic or multinational corporations interfere in the governmental relations of foreign countries is good; and to the extent if we do that I would agree, yes.

I do not agree that the bill needs to go down to ordinary and reasonable business transactions.

Mr. FEATHERMAN. I will take that stance as well on 708 because I feel that we have to do today and we have to operate in today's world.

If we are going to look ahead 10 years from now the long range planning probably will not come about because there are changes in administration and there are changes in the view of business and I think we have to operate on more or less a short-term basis at this time.

The world is getting smaller and we do have to export and not present an isolationist type of view. I believe in free trade, I believe that there is a lot of business out there for small businessmen to get.

I believe there is a lot of business out there for big businessmen to get, too.

I would like to see less restrictions so that their hands are not tied when they do export, and they can be competitive on the world market. Of course, I have to agree that what our Government laws are, I think as business people, we have to maintain and adhere to them, but I feel that there should be some middle ground where if the direction is for us to export and ship worldwide that we be given encouragement and we look at less sanctions if we do get into fields that are questionable, that we have a court of last resort we can go to before we make a decision not to take an order.

Perhaps something can be set up on a governmental level where we can go to somebody and get a ruling and a fast track ruling rather than something that takes months and years and then the opportunity slips by.

Mr. WIRTH. Gentlemen, thank you very much. As you know, I have been concerned as I think all the members of this subcommittee have been concerned, about the statements made by business people that there are ambiguities in the 1977 act which cause some pause on behalf of people when they get involved in international markets.

The next panel will get into specifics of that language and whether or not the Senate language clarifies that act or replaces one ambiguity for another.

It seems to me it doesn't do anything except enact legislation and make everybody feel good about the problem. If we create more ambiguities we give more jobs to the lawyers and accountants who can advise small business and other business people they shouldn't trade overseas because this language might get you in trouble. That gets us right back here next year or the year after, and I am not sure that members of the subcommittee, or you, or anybody else, want to address the issue again.

If we change it, let's do it right and sort it out. That is what we are concerned about.

We will get into that with the next panel. Thank you all very much for being here. We appreciate your help. We look forward to working with you.

Our next panel is Mr. John Subak, group vice president, general counsel of Rohm & Haas in Philadelphia; Mr. Robert Runser, vice president and controller of the Signal Companies in La Jolla; and Mr. Jack Richards, vice president of government affairs for the M. W. Kellogg Co., which is a subsidiary of Wheelabrator-Frye in Washington, D.C.

Gentlemen, thank you for coming in, we appreciate your appearance and we are looking forward to your testimony concerning the

Foreign Corrupt Practices Act and the alleged ambiguities in that statute and where we ought to go from here.

You are aware of the procedures of the subcommittee. We hope you can summarize your testimony in whatever way you think to be most helpful.

Your testimony will be included in the record in full with whatever other documents you may wish to provide to the subcommittee.

Mr. Subak.

STATEMENTS OF JOHN T. SUBAK, ON BEHALF OF EMERGENCY COMMITTEE FOR AMERICAN TRADE AND ROHM & HAAS CO.; ROBERT J. RUNSER, VICE PRESIDENT AND CONTROLLER, SIGNAL COMPANIES, ALSO ON BEHALF OF EMERGENCY COMMITTEE FOR AMERICAN TRADE; JACK RICHARDS, MEMBER, ACTION COMMITTEE, INTERNATIONAL ENGINEERING & CONSTRUCTION INDUSTRIES COUNCIL

Mr. SUBAK. Thank you very much, Mr. Chairman.

I am here on behalf of our company, Rohm & Haas Co., as well as the Emergency Committee for American Trade [ECAT].

Both of us support S. 708 as passed by the Senate. I don't think it is the most elegant articulation of the law, but it was passed and it is pretty good and I think by and large it cures the principal problems that we at least see in the Foreign Corrupt Practices Act.

Just a word about Rohm & Haas, we are a medium-sized chemical company, we wish we had the political clout of small business.

Our sales are just under \$2 billion, about a third outside the United States, two-thirds in the United States, we employ about 13,000 people.

ECAT represents about 61 companies with sales of \$700 billion and 5 million employees with, again, a heavy emphasis on exports.

Mr. Collins, I might add that our biggest plant is not in Dallas but in your State.

Mr. WIRTH. I think if it is not in Dallas or Mr. Collins' district, it wouldn't be of concern to him.

Mr. SUBAK. But occasionally we have heard he takes a more expansive view of things.

I guess the question I was asked to address is has the FCPA hurt American companies and would S. 708 help?

I think the answer to both of those questions is "Yes." First of all, just in the sheer paperwork mess that the act has created. We have adopted at Rohm & Haas a system to document our internal controls. That is not to say that we have increased our internal controls, we have just gone out to prove what we already had and that involved adding about a third of the people to our internal audit staff. We are no better than we were before.

We have created a few jobs, it has cost us a bunch of money and it is sheer nonsense. S. 708 would at least introduce a cost-benefit standard into the law, a standard which the law clearly needs.

In the bribery area, I think the most troublesome section is the one that was addressed by the prior panel, namely, the having-reason-to-know standard, which has led our company and other companies to walk away from business.

Essentially we are willing to be judged by our own actions. We are willing to be liable for what we do. We find it very uncomfortable to be judged by the actions of others. That discomfort increases substantially when the standard is "having reason to know," a standard with which, I think, an American businessman who wants to comply with the law should not be faced.

I have been asked once or twice before, well, OK, Subak, you say your company walked away from some business, put a number on it. That is tough.

But we have tried it. Our numbers are not precise but we are guessing that by refusing to do business in certain countries and by walking away from certain specific contracts we lost in the range of \$15 to \$20 million a year of business.

What I want to emphasize is this is not business for which we would have to pay a bribe, this is business where we feel the ambiguity of the present law puts us at risk and it is a risk we are unwilling to take.

S. 708, as I said, is not perfect but it does make us liable for our own acts and not for the acts of others.

It provides that we are liable for acts of others only if we direct or authorize a bribe. We are obviously not going to do that and, therefore, we feel that we would again be in control of our own destiny.

The third area is the one with respect to token payments. This is the question raised before, the Lagos example which is a pretty good one. The present law does not define token payments but instead it excludes from the definition of governmental employees those whose duties are essentially ministerial or clerical.

My problem with it is that I have never seen somebody wear a sign which says "my duties are essentially ministerial or clerical."

Back when I first saw the damn law I looked it up because I thought they were talking about ministers. Indeed, it would be fairly insulting to somebody to define their duties as essentially ministerial or clerical, so you really can't even ask them whether they fit the test.

The new law, S. 708, if passed, would address this issue. It would permit any facilitating or expediting payment to secure performance of a routine governmental action by a foreign official.

Again, not perfect wording but at least it gets away from a perfectly ridiculous definition of a job that nobody has ever claimed to hold.

For example, at Rohm & Haas each year, we prepare a list of the 100 or more Christmas gifts in Japan that we give to the postman, to the clerk of the court, to the clerk of city hall, to the clerk of Congress, God knows to whom else.

In each case I have the fairly foolish job of satisfying myself that each recipient of those gifts performs duties which are essentially ministerial or clerical.

S. 708 would permit gifts which are essentially a courtesy, which I think those are. It would permit gifts that are lawful in a foreign country.

I believe, Mr. Chairman, you were asking whether the act defines ministerial or clerical. It does not.

In summary, I hope that S. 708 will pass.

I don't think that it is a green light for any corrupt practices; quite the contrary.

I think that it is a clarification of a fairly confusing law and one which I trust that your panel, your subcommittee, and your committee will support.

Thank you very much.

[Mr. Subak's prepared statement follows:]

WRITTEN STATEMENT

by

John T. Subak

Group Vice President and General Counsel
Rohm and Haas Company

SUMMARY

My name is John T. Subak, and I am Group Vice President and General Counsel of the Rohm and Haas Company. I am today appearing as a witness for the Emergency Committee for American Trade ("ECAT") and for Rohm and Haas.

Rohm and Haas Company and ECAT support S.708, the Business Accounting and Foreign Trade Simplification Act, as passed by the Senate in November 1981. S.708 amends the Foreign Corrupt Practices Act of 1977 (the "FCPA"). In particular, we support the deletion of the vague "reason to know" test under the FCPA.

ROHM AND HAAS COMPANY

Rohm and Haas is a medium-sized manufacturer of specialty chemical products (polymers, resins, monomers, plastics, industrial chemicals and agricultural chemicals). It has over 13,000 employees around the world (9,000 in the United States) and has subsidiaries or affiliates and manufacturing locations in twenty countries. In 1981, the Company had sales of \$1.885 billion, approximately 65% in the United States and 35% abroad. Most of the Company's competitors are larger chemical companies, many located in Europe and Japan. In March 1976, the Company filed with the SEC a 10-K report summarizing approximately \$750,000 of improper or questionable payments made by its foreign subsidiaries during the five-year period 1971 - 1975.

ACCOUNTING STANDARDS

The FCPA as it now stands mandates internal accounting control requirements that go far beyond traditional control systems designed to assure the accuracy in all material respects of financial statements. For example, the accounting provisions of FCPA apply to every transaction of the company and its subsidiaries, whether foreign or domestic and whether or not related to the kinds of payments proscribed by the anti-bribery provisions. This places great burdens on internal auditors to document and maintain separate international accounting systems and separate sets of controls. The required paperwork is amazing. Indeed, the expense often exceeds the amounts to be controlled. These parallel accounting systems are thrust on a company without regard to cost-benefit considerations. Thus, Rohm and Haas was forced to develop and maintain an additional set of procedures and controls to audit for non-material amounts at a cost that cannot be justified.

S.708 stops short of accepting a materiality standard. Instead, in speaking of "reasonable assurances" and "reasonable detail", it adopts a prudent man standard, including a cost-benefit analysis. This is not an elegant articulation, but in recognizing that a cost-benefit analysis is appropriate, S.708 makes substantially more accounting sense than the present FCPA. Accountants are used to applying cost-benefit standards; recognizing them in the statute is a major improvement.

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THE ANTI-BRIBERY PROVISIONS

The bribery of government officials - foreign or U. S. - is wrong. It is detrimental to American foreign policy interests as well as the long-range business interests of American companies. S.708 would continue the prohibitions against bribery while removing some of the unrealistic requirements that substantially increase the cost of doing business by U. S. companies.

To cite one example:

The FCPA prohibits payments by a company to "any person, while knowing or having reason to know" that a foreign official will ultimately receive the payment. Under this vague and broad standard, liability can be imposed on a U. S. company which had no intention to make an improper payment. "Having reason to know" of improper conduct by an agent or distributor in a foreign country is the wrong test for a criminal penalty imposed by U. S. law.

S.708 focuses on the problem in a more rational manner. The U. S. company is held liable for the acts of its agents, distributors and affiliates if it expressly or by a course of conduct directs or authorizes the corrupt payment.

To cite another example:

In passing the FCPA, the Congress recognized that certain so-called token gifts or gratuities would not violate the law, yet the Act contains no statutory exemption for these payments. S.708 cures this deficiency by specifically excluding payments to secure "routine governmental action".

CONCLUSION

The FCPA is too vague and too broad. The fact that few cases have been brought under it is no solution. Law-abiding U. S. companies are entitled to clear laws; they should not have to rely on prosecutorial discretion.

The FCPA should be amended. Rohm and Haas Company and ECAT support S.708. It is not perfect, but it addresses and cures the principal problems of the FCPA. We urge prompt House passage.

June 7, 1982

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Mr. WIRTH. Thank you, Mr. Subak.

STATEMENT OF ROBERT J. RUNSER

Mr. RUNSER. Mr. Chairman, Mr. Collins, I am Robert Runser with the Signal Companies out in California, headquartered in LaJolla. I am also here testifying not only on behalf of my company, but for ECAT. I am going to emphasize the improvements as I see it through S. 708 or even Mr. Rinaldo's proposed legislation that greatly relieves some of the language problems in the original act, the FCPA. It is a fairly simple problem that I feel has been cleaned up as I will point out to you.

I spent about 10 years in public accounting. I have had a lot of practical experience and background not only in accounting matters, but in internal control matters.

I spent the last 16 years with the Signal Cos., and I have also been very involved in the formulation of legislation leading to the 1977 act that we have now together with oversight hearings by the Senate, legislative hearings by the Senate, and now I am privileged to be here before your group that is considering this issue from the other side of the aisle.

I would make an observation there has been an awful lot of time and effort put into this. We have to think a little bit, I think, about cost-benefit relationships.

I will give you an idea of why consideration of amending the FCPA is so important to a large company like Signal.

We are very diversified; in 1981, we had over \$5 billion in sales, about 5.5, but very diversified. About 34 percent of our 1981 sales was in the foreign arena. About roughly half of it was export business and the other half was what we call foreign source business where products are manufactured and sold abroad, so I think you can see how interested we are in moving ahead with a workable kind of FCPA.

Another thing I want to briefly describe to you to maybe help illustrate to you that large corporations in this country I don't think take the FCPA lightly at all.

I think we heard in the very fine testimony from the small business people that they have real concerns before they make decisions.

They back off rather than make a decision they are afraid they will be hung with on legal liability because of ambiguities later on.

We are able to operate within the environment of the FCPA because of our environment at the Signal Cos.

We have an audit committee which is the extension of our board of directors. They are very concerned that we don't do the wrong thing. They are concerned about integrity of financial statements and propriety and maintenance of proper controls so there are not unlawful, illegal kinds of transactions.

We extend our thinking, quite frankly, beyond the foreign arena to domestic operations.

Illegal kinds of things in our domestic operations are just as much a no-no as in foreign.

I just briefly described that to you to give you an example that I think may, in many corporations, the large percentage in this

country, are really making a sincere effort to comply with the FCPA, so how can we make it a little easier to comply?

Chairman Wirth, you asked a very good question at the start here. Where is the FCPA language unclear? I am going to simply point that out to you.

In the original law there are words in there that talk about accurate and detailed accounting records, and what happened when that legislation came out that way, it spooked all the accountants in private industry, the public accountants, lawyers, everyone else, as to what accurate and detailed records mean.

In the real world I can assure you there is no such thing as an absolutely accurate and detailed accounting record. There are a lot of judgments and estimates involved. Former Chairman of the SEC, Harold Williams, in January 1981, made what I thought was a very good run at defining what recordkeeping meant, and he got back to the terms "reasonableness" and "fairness" to describe those records, but it was very interesting he omitted any reference to "accurate" in his testimony.

I think just removing any connotation that accounting records are detailed or accurate—which S. 708 and Congressman Rinaldo's proposal basically do—is a very small but a very large move in the right direction to remove a lot of uncertainty in the accounting arena at least.

The second point I would like to make is, I think the reasonableness test included in 708 as defined by a prudent man in the conduct of his own affairs comes out loud and clear in all the proposals.

I think that is good because that allows good faith businessmen to exercise their judgment, depending upon the given business circumstances, and this idea of reasonableness goes to the detail of the accounting records, but also to the reasonable assurance of the internal controls surrounding those records, so you get back to reasonableness and a prudent man kind of test which quite frankly we in the business world think was the intent of Congress in the first place.

I don't think they intended to change the long historical definition of internal controls. This has been with us for years and years. It is a daily responsibility of ours to be sure our records don't fall apart.

Mr. WIRTH. If I might just respond to that, I agree with what you have said, too, Mr. Subak, about the accounting area.

Mr. RUNSER. Yes.

Mr. WIRTH. If you look at the language from the Senate report 1977, there was no intent to get it down to the exactitude that you were suggesting. The committee report says:

The committee recognizes, however, that management must exercise judgment in determining the steps to be taken and the cost incurred—

Cost-benefit, Mr. Subak—

In giving assurance to the objectives expressed will be achieved. Here standards of reasonableness must apply. In this regard the term "accurately" does not mean exact precision as measured by some abstract principle.

I think this reflects what both of you were saying. I think if it is as apparent that the report language was not adequate to assure

the accountants or the internal audit committees that you all have to deal with, then putting that in the legislative language would be a very real improvement.

Mr. RUNSER. To get accuracy out of the legislative language.

Mr. WIRTH. Isn't that what the Senate has done and what was the intent all along? Let's make it clear that "exact precision" is not required, but that standards of reasonableness apply.

Mr. RUNSER. Instead of having it in a supplemental document here, let's get it out of there.

Mr. WIRTH. Let's say we agree on the accounting materials.

Again I am trying to sort this through. You say why do you spend all this time doing it? If we are going to do it, let's do it right. It seems that is one of the responsibilities we ought to have.

As I suggested earlier, there is a tendency up here to legislate for the purpose of legislating. That may not do the job for you year out.

Let's assume on the accounting side what has been proposed in the Senate makes a good deal of sense. Now, let's get over to where the other ambiguities exist, Mr. Runser.

Mr. RUNSER. I just want to make one more comment that is in the accounting section and then I am going to defer to Mr. Subak and Mr. Richards here because I am here to speak strictly about accounting.

I can make comments later on in answering questions about other aspects. I am not an expert in that area.

The other thing that really frightened businessmen with this detailed, accurate kind of wording that was in the language was, well, what is our liability if something happens?

What if we discover a control weakness? Is the SEC and the Justice Department going to be all over us, or how are they going to conduct themselves? Will we end up in jail?

There was a lot of confusion. So the introduction of the scienter provision in Rinaldo and S. 708 is really a great step forward because here is the way I see it:

If you discover, if a corporation discovers a control weakness, the most important thing—and I am assuming there is no collusion or no full involvement—when they discover it, the most important thing is to do something about it and take action to correct the situation, discipline, if necessary; whatever.

I think any prudent man would reasonably say if you conduct yourself that was as a businessman, there is no way that we should be charged with liability, with civil or criminal liability.

I think that was a giant step forward in all of the deliberations. So the bottom line, I don't think that Rinaldo or S. 708 basically changes the thrust of the FCPA which is quite frankly to prohibit bribery. That is the main thrust.

I don't think—they may have inadvertently ended up this way, but I don't think Congress or anybody was trying to discourage foreign business or eliminate foreign business.

It is a problem, but we can consider it in other ways.

Why let accounting ambiguities constrain us in our business conduct rather than faith as act in God reasonably prudent man. Let us in the private sector exercise our judgment subject to oversight by the Congress and the Justice Department.

I think that is about enough remarks.

[Mr. Runser's prepared statement follows:]

STATEMENT OF ROBERT J. RUNSER, VICE PRESIDENT AND CONTROLLER
THE SIGNAL COMPANIES, BEFORE THE SUBCOMMITTEE ON TELECOMMUNICATIONS,
CONSUMER PROTECTION, AND FINANCE, OF THE HOUSE ENERGY AND COMMERCE COMMITTEE
OVERSIGHT HEARINGS ON THE FOREIGN CORRUPT PRACTICES ACT

Tuesday, June 8, 1982

Mr. Chairman, members of the Committee, my name is Robert J. Runser, and I'm Vice President and Controller of The Signal Companies headquartered in La Jolla, California. I am here today on behalf of the Emergency Committee for American Trade to briefly testify and, more importantly, answer your questions regarding the accounting standards section of the Foreign Corrupt Practices Act.

A little background for you as far as my experience is concerned. It represents 11 years in public accounting with a major accounting firm and in the last 16 years as the chief accounting officer at The Signal Companies. I have also been very involved in many accounting issues, including the Foreign Corrupt Practices Act, over recent years, through my activities in the Financial Executives Institute and my dealings on the conceptual framework task force with the Financial Accounting Standards Board.

A brief profile of The Signal Companies: We are a very large, diversified company. Our sales last year were in excess of \$5 billion. Approximately 15 percent of those consolidated sales represent what we call "foreign source business." Another 10 percent of our revenues come from export business.

So, I think this gives you a clear indication of how vitally concerned we are with legislation that would clarify the FCPA.

2.

One other point of Signal's profile so you will get a better insight into some of my answers to your questions, we are very aware of the importance of our internal control environment. That environment is represented by a written policy charter of our audit committee, which is an extension of our board of directors. The grassroots of that policy are integrity of the financial information to external users, and independence and free access to external auditors, internal auditors, and all levels of management to our audit committee.

I think you can see we take the matter of the FCPA very seriously in our company. We also strongly support the proposed amendments to the Foreign Corrupt Practices Act, primarily because they would relieve a lot of unnecessary ambiguities and uncertainties that exist in the current legislation.

First of all, I think they remove what I see, from an accounting viewpoint, as the greatest uncertainty in the Foreign Corrupt Practices Act language, namely the use of the words "accurate records."

I can assure you there is no such animal that exists on the face of the Earth. It is impossible to have literally accurate and precise records.

In Chairman Williams' speech to the American Institute of Certified Public Accountants (AICPA) on January 13, 1981, he broadly defined recordkeeping. He used the words "reasonableness" and "fairness" to describe such records but he omitted the word "accurate."

3.

The Rinaldo bill and the Senate bill would both use the "reasonableness" concept. It is a very positive step in removing a lot of uncertainty as far as the accounting provisions are concerned.

Second, I think the reasonableness test, as defined by a prudent man in the conduct of his own affairs, is clearly expressed in the proposed amendments. It goes to not only the reasonable detail of accounting records, but also to the reasonable assurance of internal controls surrounding such records.

The third point I want to make is that the proposed amendments to the FCPA properly recognize scienter as a basic ingredient in managements' conduct of their daily business responsibilities. If a control breakdown is discovered by management, which then takes prompt action to correct the situation, it seems reasonable that a prudent man would not charge management with civil and criminal liability.

In summary, before welcoming your questions, I would simply say that H.R. 2530 and S. 708 as passed by the Senate after lengthy and careful consideration go a long way toward eliminating unnecessary ambiguity. These bills do not, in my view, basically change the principal thrust of the FCPA. Foreign bribes are still a no-no.

The basic question is why should business be constrained in conducting its operations because of gross ambiguities in accounting terminology, particularly when these ambiguities can be clarified without prejudice to the purposes of the FCPA.

Let us, as businessmen, design accounting and control systems that are workable, responsive to the law, and help the government enforce the law. The proposed amendments to the FCPA before the House would basically accomplish this.

I would now be pleased to address any questions you may have in the accounting standards section of the FCPA.

Mr. WIRTH. Let me ask you while we are still on this, in the area you wanted to focus on about the criminal penalties, how does what is in the FCPA now differ in terms of penalties from what you, the accountants, the audit trail, and so on, are subject to under other statutes?

Mr. RUNSER. It answers the question, I think, that there is liability for knowing violations in the current.

Mr. WIRTH. Isn't that willful violation?

Mr. RUNSER. That is right. For willful, knowing violations; but it is unclear in the act of 1977.

What about in the case of inadvertent kinds of violations? What do you do in the case where you discover a control breakdown? Do you have any liabilities? It is unanswered.

Mr. WIRTH. I think it is pretty clear that you don't have a criminal liability in that case.

The only time criminal penalties are brought to bear under the accounting provisions of the 1977 act is when the Justice Department finds that there were willful violations. The statute says that.

Mr. RUNSER. Is that in the legislation?

Mr. WIRTH. I believe it is.

Mr. RUNSER. You and I are having a good dialog here, but doesn't it illustrate the ambiguity of it and the unclearness of it? Why not make it clear?

Ms. COCHRAN. Let me address that.

Section 32 of the Securities and Exchange Act of 1934 provides that willful violations of any provision of the Exchange Act—

Mr. RUNSER. Here we are talking about something outside the 1977 FCPA. Why not make it clear by amending the FCPA?

Ms. COCHRAN. Just to make it clear for the record, the FCPA is found in section 30A of the Exchange Act. Section 32 applies to any violations of the Exchange Act and says that only if the violation is "willful" can you be prosecuted criminally. Even "willful" violations of the margin provisions of the Exchange Act can be prosecuted criminally. It is very consistent with the whole scheme of the Exchange Act.

Mr. RUNSER. I am sorry I am not a lawyer. To me the secret to communications is making it so simple and understandable there won't be misunderstanding.

Mr. WIRTH. Therefore, could you take the language from section 32 of the Exchange Act and write that into the FCPA provisions, to say that the only time there is criminal prosecution is, when the Justice Department finds there is a willful violation.

Do that rather than refer to some other section which you and I as nonlawyers go nuts trying to figure out. Would that not do the job?

Mr. RUNSER. I guess the way I would answer your question, Mr. Wirth, is yes, you are having your hearings here. I don't quite know what—we are not looking at proposed legislation here. You are trying to get input. What I would say to you is, why do we reinvent the wheel when it has basically been done by Rinaldo and S. 708? That I don't understand as a layman.

Mr. WIRTH. Now—

Mr. RUNSER. What the language in S. 708—that is fine.

Mr. WIRTH. Let me point out why I brought that issue up.

The Securities and Exchange Commission has jurisdiction over this area under the 1977 act; that if there are willful violations of the law under the Securities and Exchange Act of 1934, law, then there can be criminal penalties.

Under S. 708, that part of the SEC jurisdiction is decriminalized.

My question is, Why are some SEC violations which are willful criminalized and others not? Why not make it consistent and say if there are willful violations of the FCPA, like other areas under the 1934 Securities Act, willful violations come with criminal prosecution.

There hasn't been any problem in 50 years of SEC jurisdiction.

Mr. RUNSER. Conceptually I think we are pretty much in agreement, as long as it is clarified that unless there is willfulness, that you don't have a liability if you take care of it. Let's get on with it and do it.

Mr. WIRTH. We are making a lot of progress. That is great.

Mr. RUNSER. If you want to put up something for every view, fine.

Mr. WIRTH. The whole purpose of what we are trying to do is say let's legislate in a clear fashion so everybody knows what the expectations are and aren't.

Mr. RUNSER. I am saying basically that is pretty much done already. We are almost there.

Mr. WIRTH. I just wanted to pin down that one point where there is the criminal prosecution issue which is dropped in S. 708. It seemed to me it is mutually exclusive from the basic intent of the 1934 act.

Let's make that consistency there and make it clear, as you are suggesting; put that language very clearly in the statute that says willful violation. You solved the problem.

Everybody knows what we are talking about. You are not talking about a mistake or something like that. You have to have the Justice Department find a willful violation in order to have criminal liability.

None of us wants to have that. Nobody is saying we want a willful violation of law that goes untouched.

Mr. RUNSER. Our neck is on the line every day on this issue.

STATEMENT OF JOHN RICHARDS

Mr. RICHARDS. I am Jack Richards, vice president of government affairs of the Kellogg Co., which is a subsidiary of Wheelator Frye. I am testifying today on behalf of the International Engineering and Construction Industries Council, called IECIC.

I am currently a member of the IECIC action committee.

This group is composed of the American Consulting Engineers Council, the Associated General Contractors of America, the National Constructors Association, and the American Institute of Architects.

Together these organizations represented on the order of 15 billion dollars' worth of design and construction work last year, thus contributing significantly to the positive components in the U.S. balance of trade.

IECIC welcomes this opportunity to discuss the problems with the present application of the Foreign Corrupt Practices Act of 1977. We feel strongly the need to express our views for amending legislation similar to language passed by the Senate in S. 708 which clarifies the law without diminishing the original intent of the act to outlaw bribery.

Let me say I compliment the committee and the staff for getting this panel together of three individuals very interested in the impact of this law. We have a lawyer, an accountant, and an engineer. All of us are impacted. We have real problems.

Mr. WIRTH. Mix that up with politicians and make a mess of the whole thing.

Mr. RICHARDS. At the outset I must say very positively we don't believe in bribery of foreign officials as a way of doing business. The IECIC companies and my own company are well-established, reputable leaders in the engineering-construction industry and we cannot afford the ramifications of illicit payments.

We have strong reputations and we consider illicit payments unethical and not in the best interests of the U.S. exports of goods and services.

The committee has held several days of oversight hearings, and we won't go into more detail on some of the issues.

I would like to make the point we wish to clarify the ambiguities of the law and to modify its application in a manner more consistent with the realities of the highly competitive international marketplace.

The act, in its current form, is so vague that many American firms uncertain of its application are declining to engage in many legitimate activities that they fear may be challenged.

Moreover, unclear enforcement priorities of administering the law add substantially to this uncertainty.

You are well aware of the arguments, I believe, made by various business groups with regard to the excessive and unrealistic accounting and reporting standards.

Mr. Runser on my left has laid these before you. The ambiguities of the bribery provisions have been covered and will be covered in questions and answers by Mr. Subak.

We believe both of these issues are addressed thoroughly in the proposed legislation.

I understand the committee has expressed an opinion that there is little hard evidence that the U.S. business has been affected by this law.

My reason for being here today, Mr. Chairman, is to assure you that the IECIC companies and U.S. industry are affected. Having spent more than 21 years of my 37-year career overseas in engineering and construction activities, I know that many U.S. firms are reluctant to undertake projects in many countries because of their concern over the application and associated penalties of the law.

The law in its present form will continue to serve as a deterrent to engineering and construction exports until it is restructured to address the practical needs of our industries.

I wish I could tell you precisely that U.S. industry in any given year lost x billion dollars' worth of business. Unfortunately, there

are many contributing causes for lost U.S. exporting business and it is extremely difficult, often impossible, in every case to distinguish the primary reason for a lost contract.

I agree there is not a single reason for loss of export business. There are many, many disincentives. This is a law we believe can be passed to remedy the present situation.

We understand the committee has also seen the report by the International Division of the Chamber of Commerce of the United States of America entitled "The Price of Ambiguity: More Than Three Years Under the Foreign Corrupt Practices Act."

I participated in the task force that prepared this document which gives many examples of lost business attributable to the present law.

In our opinion the evidence of lost business is there for those who care to see it.

I would like to distinguish three separate aspects of the law's impact on U.S. exports: The first involves an unwillingness on the part of U.S. firms to engage in commercial arrangements such as joint ventures in countries whose routine business practices may be challenged under the FCPA. This particular problem has been experienced in Australia where some 800 U.S. companies operate.

The Australian Government has complained bitterly that the FCPA is costing it export income. This is an example of the reaction by a foreign government to the law and a consequent loss of opportunity for U.S. business.

The second example involves uncertainty—or a second series of examples, involves uncertainty in the definition of facilitating payments under the law.

Mr. McGeedy, in the earlier testimony, gave two very current and good examples of this. In any eastern country personal payments are expected from most routine services, such as the arranging of appointments, providing customs protection for equipment.

One of the previous panelists has mentioned moving materials through Customs on a timely basis. Uncertainty over the law's treatment of such payments has caused many companies to withdraw completely from activities in these countries.

Another aspect of the problem involves a reluctance to adapt to foreign customs because of the law's impact.

For example, it is uncertain how we can provide customary gifts and entertainment and other social accommodations that have become a large part in developing and maintaining friendly relationships between the business community and foreign governments.

In fact, many of the things that are legislated under the present law are done in this country and considered to be legitimate, but are considered under the law to not be so.

I have listed some of those in my formal testimony. There are examples of practices which many companies have stopped because of a concern of violating the FCPA.

Lastly, we think it is unreasonable to hold U.S. firms responsible for the actions of third party intermediaries which they are required by local law to employ.

There are numerous examples of opportunities which were not pursued by U.S. companies because they could not be certain of third party compliances with our law.

One such example involved a major U.S. corporation which declined a substantial subcontract in an African country because of the possibility of an indirect payment to government officials in that country through the prime contractor.

The subcontract was subsequently awarded to a European competitor unencumbered by a statute like the FCPA.

We have extreme difficulty supporting a law which prevents U.S. industry from following reasonable business practices in foreign countries in respect of gifts, entertainment, travel and other social amenities.

This is particularly unreasonable and inconsistent in the light of the legitimate acceptance in this country of the same practices by U.S. Government officials.

For this reason alone, a case exists for amendment of the present law.

Mr. Chairman, I hope we have provided the committee additional evidence which, combined with the past legislative development on this issue, supports the urgent need for amendments to the FCPA.

We think amending this legislation is of extreme importance to our industry and represents a major step in our overall effort to improve exports from the USA. We therefore support and urge the committee to consider favorably the adoption of amending FCPA legislation consistent with the general provisions of H.R. 2530 and the final S. 708.

Thank you for this opportunity to appear before the committee and I will be pleased to try to answer any questions.

[Mr. Richard's prepared statement follows:]

TESTIMONY OF
JACK RICHARDS

FOR

THE INTERNATIONAL ENGINEERING AND CONSTRUCTION INDUSTRIES COUNCIL

MR. CHAIRMAN, MEMBERS OF THE COMMITTEE:

MY NAME IS JACK RICHARDS AND I AM VICE PRESIDENT FOR GOVERNMENT AFFAIRS OF THE M. W. KELLOGG COMPANY, A SUBSIDIARY OF WHEELABRATOR-FRYE, INC. I AM TESTIFYING HERE TODAY ON BEHALF OF THE INTERNATIONAL ENGINEERING AND CONSTRUCTION INDUSTRIES COUNCIL (IECIC) IN MY CURRENT CAPACITY AS A MEMBER OF THE IECIC ACTION COMMITTEE, THE IECIC IS COMPOSED OF THE AMERICAN CONSULTING ENGINEERS COUNCIL, THE ASSOCIATED GENERAL CONTRACTORS OF AMERICA, THE NATIONAL CONSTRUCTORS ASSOCIATION AND THE AMERICAN INSTITUTE OF ARCHITECTS. TOGETHER THESE ORGANIZATIONS REPRESENTED ON THE ORDER OF \$15 BILLION WORTH OF DESIGN AND CONSTRUCTION WORK LAST YEAR, THUS CONTRIBUTING SIGNIFICANTLY TO THE POSITIVE COMPONENTS IN THE U. S. BALANCE OF TRADE.

IECIC WELCOMES THIS OPPORTUNITY TO DISCUSS THE PROBLEMS WITH THE PRESENT APPLICATION OF THE FOREIGN CORRUPT PRACTICES ACT OF 1977. WE FEEL STRONGLY THE NEED TO EXPRESS OUR VIEWS FOR AMENDING LEGISLATION SIMILAR TO LANGUAGE PASSED BY THE SENATE IN S. 708 WHICH CLARIFIES THE LAW WITHOUT DIMINISHING THE ORIGINAL INTENT OF THE ACT TO OUTLAW BRIBERY.

AT THE OUTSET, LET ME STATE, POSITIVELY, THAT WE DO NOT BELIEVE BRIBERY OF FOREIGN OFFICIALS IS AN ACCEPTABLE WAY OF DOING BUSINESS. COMPANIES REPRESENTED BY THE IECIC ASSOCIATIONS ARE WELL-ESTABLISHED, REPUTABLE LEADERS IN THE ENGINEERING-CONSTRUCTION INDUSTRY WHO CANNOT AFFORD THE CERTAIN RAMIFICATIONS OF ILLICIT PAYMENTS AND THE ACCUSATION OF INAPPROPRIATE OR ILLEGAL BUSINESS TRANSACTIONS. OUR MEMBERS HAVE DEVELOPED THEIR STRONG REPUTATIONS IN WORLD MARKETS BY OFFERING A BETTER PRODUCT, SOPHISTICATED TECHNOLOGIES AND BY ESTABLISHING THEMSELVES AS RESPONSIBLE BUSINESS PARTNERS. WE CONSIDER ILLICIT PAYMENTS UNETHICAL AND NOT IN THE BEST INTERESTS OF U. S. EXPORTS OF GOODS AND SERVICES.

SINCE THIS COMMITTEE HAS ALREADY HELD SEVERAL DAYS OF OVERSIGHT HEARINGS ON THE FOREIGN CORRUPT PRACTICES ACT (FCPA), LET ME TALK SPECIFICALLY ABOUT THE PROBLEMS OUR INDUSTRIES HAVE WITH THE CURRENT LAW. IECIC JOINS OTHER BUSINESS GROUPS IN SEEKING

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TO CLARIFY THE AMBIGUITIES IN THE LAW AND MODIFY ITS APPLICATION IN A MANNER MORE CONSISTENT WITH THE REALITIES OF THE HIGHLY COMPETITIVE INTERNATIONAL MARKETPLACE. THE FOREIGN CORRUPT PRACTICES ACT, IN ITS CURRENT FORM, IS SO VAGUE THAT MANY AMERICAN FIRMS, UNCERTAIN OF ITS APPLICATION, ARE DECLINING TO ENGAGE IN MANY LEGITIMATE ACTIVITIES THAT THEY FEAR MAY BE CHALLENGED. MOREOVER, THE UNCLEAR ENFORCEMENT PRIORITIES OF ADMINISTERING THE LAW ADD SUBSTANTIALLY TO THIS UNCERTAINTY. IT IS THESE AND OTHER MATTERS THAT NEED TO BE ADDRESSED.

MR. CHAIRMAN, YOU ARE WELL AWARE OF THE ARGUMENTS MADE BY VARIOUS BUSINESS GROUPS WITH REGARD TO THE EXCESSIVE AND UNREALISTIC ACCOUNTING AND REPORTING STANDARDS MANDATED BY A STRICT INTERPRETATION OF THE FOREIGN CORRUPT PRACTICES ACT. WE BELIEVE THAT THE HISTORY OF THE AMENDING LEGISLATION TO DATE HAS ADEQUATELY ADDRESSED OUR INDUSTRY'S CONCERN ON THESE ISSUES AS SET FORTH ORIGINALLY IN H.R. 2530 AND IN THE FINAL VERSION OF S. 708.

THE AMBIGUITIES IN THE BRIBERY PROVISIONS OF THE CURRENT LAW HAVE BEEN DISCUSSED THOROUGHLY BY WITNESSES APPEARING BEFORE THIS SUBCOMMITTEE IN PREVIOUS HEARINGS. CHIEF AMONG OUR CONCERNS IS THE EXTENT TO WHICH A U. S. COMPANY CAN BE HELD LIABLE FOR THE ACTIONS OF ITS FOREIGN AGENTS OVERSEAS AND THE PROBLEMS SURROUNDING THE DETERMINATION OF AN "ILLICIT PAYMENT." WE FEEL THESE ISSUES ARE ALSO ADDRESSED THOROUGHLY IN THE PROPOSED LEGISLATION. I WILL, OF COURSE, BE HAPPY TO EXPOUND ON ANY OF THESE POINTS.

WE UNDERSTAND THE COMMITTEE HAS EXPRESSED AN OPINION THAT THERE IS LITTLE HARD EVIDENCE THAT U. S. BUSINESS HAS BEEN AFFECTED BY THIS LAW. MY REASON FOR BEING HERE TODAY, MR. CHAIRMAN, IS TO ASSURE YOU THAT THE IECIC COMPANIES AND U. S. INDUSTRY ARE AFFECTED. HAVING SPENT MORE THAN TWENTY YEARS OF MY CAREER OVERSEAS IN ENGINEERING AND CONSTRUCTION ACTIVITIES, I KNOW THAT MANY U. S. FIRMS ARE RELUCTANT TO UNDERTAKE PROJECTS IN MANY COUNTRIES BECAUSE OF THEIR CONCERN OVER THE APPLICATION AND ASSOCIATED PENALTIES OF THE LAW. THE LAW IN ITS PRESENT FORM WILL CONTINUE TO

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SERVE AS A DETERRENT TO ENGINEERING AND CONSTRUCTION EXPORTS UNTIL IT IS RESTRUCTURED TO ADDRESS THE PRACTICAL NEEDS OF OUR INDUSTRIES.

I WISH I COULD TELL YOU PRECISELY THAT U. S. INDUSTRY IN ANY GIVEN YEAR LOST X BILLION DOLLARS BECAUSE OF THE PROVISIONS OF THE LAW. UNFORTUNATELY, THERE ARE MANY CONTRIBUTING CAUSES FOR LOST U. S. EXPORT BUSINESS, AND IT IS EXTREMELY DIFFICULT, OFTEN IMPOSSIBLE, IN EVERY CASE TO DISTINGUISH THE PRIMARY REASON FOR A LOST CONTRACT. THIS POINT WAS MADE AT THE SIXTH IECIC ACTION CONFERENCE LAST OCTOBER IN WASHINGTON BY MANY CONGRESSIONAL AND ADMINISTRATION OFFICIALS. THE REPORT OF THAT CONFERENCE WHICH RECOMMENDS AMENDMENT OF THE LAW HAS BEEN SENT TO EVERY MEMBER OF THIS COMMITTEE.

WE UNDERSTAND THE COMMITTEE HAS ALSO SEEN THE REPORT BY THE INTERNATIONAL DIVISION OF THE CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA ENTITLED THE PRICE OF AMBIGUITY: MORE THAN THREE YEARS UNDER THE FOREIGN CORRUPT PRACTICES ACT. I PARTICIPATED IN THE TASK FORCE THAT PREPARED THIS DOCUMENT WHICH GIVES MANY EXAMPLES OF LOST BUSINESS ATTRIBUTABLE TO THE PRESENT LAW. IN OUR OPINION, THE EVIDENCE OF LOST BUSINESS IS THERE FOR THOSE WHO CARE TO SEE IT.

WE DISTINGUISH THREE SEPARATE ASPECTS OF THE LAW'S IMPACT ON U. S. EXPORTS. THE FIRST INVOLVES AN UNWILLINGNESS ON THE PART OF U. S. FIRMS TO ENGAGE IN COMMERCIAL ARRANGEMENTS SUCH AS JOINT VENTURES IN COUNTRIES WHOSE ROUTINE BUSINESS PRACTICES MAY BE CHALLENGED UNDER THE FCPA. THIS PARTICULAR PROBLEM HAS BEEN EXPERIENCED IN AUSTRALIA, WHERE THE AUSTRALIAN GOVERNMENT HAS COMPLAINED THAT THE FCPA IS COSTING IT EXPORT INCOME. THIS IS AN EXAMPLE OF THE REACTION BY A FOREIGN GOVERNMENT TO THE LAW AND A CONSEQUENT LOSS OF OPPORTUNITY FOR U. S. BUSINESS.

THE SECOND EXAMPLE INVOLVES UNCERTAINTY IN THE DEFINITION OF FACILITATING PAYMENTS UNDER THE LAW. IN ONE TYPICAL INSTANCE IN SOUTH AMERICA, A U. S. BUSINESS EXECUTIVE WAS FORCED TO PAY AN EXTRAORDINARILY HIGH CUSTOMS DUTY ON HIS HOUSEHOLD GOODS. IT WAS MADE CLEAR BY CUSTOMS OFFICIALS THAT HAD THE EXECUTIVE PAID THEM A SPECIFIC AMOUNT DIRECTLY, THE ASSESSMENT WOULD HAVE BEEN SUBSTANTIALLY LESS. IN ORDER TO

AVOID ANY PROBLEMS UNDER THE FCPA, THE INCREASED ASSESSMENT WAS PAID AT A CONSIDERABLE LOSS TO THE COMPANY.

FURTHERMORE, PARTICULARLY IN ANY FAR EASTERN COUNTRY, PERSONAL PAYMENTS ARE EXPECTED FOR THE MOST ROUTINE SERVICES, SUCH AS ARRANGING APPOINTMENTS, PROVIDING CUSTOMS PROTECTION FOR EQUIPMENT AND COMPLETING OVERSEAS PHONE CALLS. UNCERTAINTY OVER THE LAW'S TREATMENT OF SUCH PAYMENTS HAS CAUSED MANY COMPANIES TO WITHDRAW COMPLETELY FROM BUSINESS ACTIVITY IN THOSE COUNTRIES.

ANOTHER ASPECT OF THIS PROBLEM INVOLVES A RELUCTANCE TO PROVIDE CUSTOMARY GIFTS AND ENTERTAINMENT AND OTHER SOCIAL ACCOMMODATIONS THAT HAVE BECOME A LARGE PART IN DEVELOPING AND MAINTAINING FRIENDLY RELATIONSHIPS BETWEEN THE BUSINESS COMMUNITY AND FOREIGN GOVERNMENTS. EXAMPLES OF THESE CUSTOMARY PRACTICES WHICH HAVE BEEN STOPPED BY MANY U. S. COMPANIES BECAUSE OF A CONCERN OF VIOLATING THE FCPA FOLLOW:

1. GOVERNMENT PURCHASING OFFICER'S EXPENSES INCURRED FOR TRIPS TO REVIEW AND EVALUATE QUALIFICATIONS, SPECIFICATIONS, DELIVERY, SCHEDULES, ETC.
2. PAYMENTS FOR EXPENSES INCURRED BY GOVERNMENT OFFICIALS REQUIRED TO LEAVE THEIR HOME AREA TO FULFILL DUTIES.
3. WRITING SPECIFICATIONS FOR EQUIPMENT FOR A GOVERNMENT WITHOUT CHARGE IN THE HOPE OF OBTAINING FUTURE BUSINESS.
4. PAYMENT OF EXPENSES INCURRED BY GOVERNMENT EMPLOYEES WHILE ATTENDING TRAINING COURSES.
5. ENTERTAINMENT OF AND GIFTS TO GOVERNMENT OFFICIALS WHERE THIS IS A USUAL PRACTICE.

LASTLY, IT IS UNREASONABLE TO HOLD U. S. FIRMS RESPONSIBLE FOR THE ACTIONS OF THIRD PARTY INTERMEDIARIES WHICH THEY ARE REQUIRED BY LOCAL LAW TO EMPLOY. THERE ARE NUMEROUS EXAMPLES OF OPPORTUNITIES WHICH WERE NOT PURSUED BY U. S. COMPANIES BECAUSE THEY COULD NOT BE CERTAIN OF THIRD PARTY COMPLIANCES WITH OUR LAW. ONE SUCH EXAMPLE INVOLVED A MAJOR U. S. CORPORATION WHICH DECLINED A SUBSTANTIAL SUBCONTRACT IN AN

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AFRICAN COUNTRY BECAUSE OF THE POSSIBILITY OF AN INDIRECT PAYMENT TO GOVERNMENT OFFICIALS IN THAT COUNTRY THROUGH THE PRIME CONTRACTOR. THE SUBCONTRACT WAS SUBSEQUENTLY AWARDED TO A EUROPEAN COMPETITOR UNENCUMBERED BY A STATUTE LIKE THE FCPA.

WE HAVE EXTREME DIFFICULTY, AND I THINK THIS COMMITTEE SHOULD ALSO IN SUPPORTING A LAW WHICH PREVENTS U. S. INDUSTRY FROM FOLLOWING REASONABLE BUSINESS PRACTICES IN FOREIGN COUNTRIES IN RESPECT OF GIFTS, ENTERTAINMENT, TRAVEL AND OTHER SOCIAL AMENITIES. THIS IS PARTICULARLY UNREASONABLE AND INCONSISTENT IN THE LIGHT OF THE LEGITIMATE ACCEPTANCE IN THIS COUNTRY OF THE SAME PRACTICES BY U. S. GOVERNMENT OFFICIALS. FOR THIS REASON ALONE, A CASE EXISTS FOR AMENDMENT OF THE PRESENT LAW.

MR. CHAIRMAN, I HOPE WE HAVE PROVIDED THE COMMITTEE ADDITIONAL EVIDENCE, WHICH COMBINED WITH THE PAST LEGISLATIVE DEVELOPMENT ON THIS ISSUE SUPPORTS THE URGENT NEED FOR AMENDMENTS TO THE FCPA.

CLARIFYING AMENDMENTS TO THE FCPA IS OF EXTREME IMPORTANCE TO OUR INDUSTRY AND WILL REPRESENT A MAJOR STEP IN THE DEVELOPMENT OF OUR U. S. EXPORT ENHANCEMENT POLICY. WE, THEREFORE, SUPPORT AND URGE THE COMMITTEE TO CONSIDER FAVORABLY THE ADOPTION OF AMENDING FCPA LEGISLATION CONSISTENT WITH THE GENERAL PROVISIONS OF H.R. 2530 AND THE FINAL S. 708.

THANK YOU FOR THIS OPPORTUNITY TO APPEAR BEFORE THE COMMITTEE, AND I WILL BE PLEASED TO TRY TO ANSWER ANY QUESTIONS.

Mr. WIRTH. Thank you very much, Mr. Richards.

Going back to where we were, I took issue with a lot of statements made last year that the Foreign Corrupt Practices Act was the major inhibitor of American trade overseas—which I thought was a little bit of rhetorical finery.

There is a general unease. I understand that.

I think that that is valid if you look at what Mr. Runser and I were talking about in the accounting provisions. An audit group would find an uneasiness about the wording. That is legitimate.

Let me, if I might, go to some of the other provisions.

One of those is the question that we were discussing earlier that Mr. Subak was talking about—"ministerial or clerical" language. Mr. Mudge was suggesting earlier that it might be insulting to somebody to say they are ministerial and clerical.

What has happened in the legislation in the Senate bill is that it has been replaced by "routine" business. It seems to me that, though I am not sure it is very clear and understandable what "routine" business is—are we having a definitional problem? Should we put "routine business" in the legislation and define that in the report as "ministerial and clerical"? What is "routine business?"

What isn't "routine business?" You could be in a situation where an audit committee or management group says well, I am not sure what is routine business. Is "routine" business bribery or not bribery?

Do you see what the interpretation could be?

I don't want to be back here 2 years from now going through this, saying, well, "routine" business isn't well enough defined and that is inhibiting us from wanting to get into foreign trade areas.

Is there a generally accepted understanding of what "routine" business is?

Mr. Subak.

Mr. SUBAK. Well, it is not a new question, obviously. It is one that has troubled the draftsmen in 1977. It came up at the SEC level.

My classmate, Stan Sporkin, for example, took very strong umbrage to a suggestion made by other people on the staff that there be a dollar definition.

People talked about allowing payments under \$500 or under \$1,000. Stan Sporkin said, well, what is the price of integrity?

That became a politically unattractive way to go.

I don't think that there is an easy solution to it. I think that ministerial or clerical is a clear loser. It defines the recipient rather than the action that is being taken. Allowing a facilitating payment to secure the performance of a routine governmental action is not deathless prose, but it is a hell of a lot better than what we have right now.

If you were starting afresh, you might use different language; I might use different language, but in the interests of substantially improving the act, I would urge sticking with that language in S. 708.

It is a tough, tough phrase to define and to define in a politically acceptable manner.

Mr. WIRTH. Do you have anything to add?

Mr. RICHARDS. I would be the last to say as a chemical engineer I am very good on the deliberations on the language of the FCPA amendments.

I think this is a sufficiently important issue that we might want to consider this through our group that has been working on this issue and come up with some—maybe some suggestions which have arisen as a result of this hearing.

Mr. WIRTH. I would really appreciate that. Again, I don't want to be back here, the members don't want to be back here readdressing this when we don't really know what "routine" business is. There is another phrase in the Senate language, something like routine governmental activity or routine governmental action.

Does that mean you know what Mrs. Thatcher does is routine government?

I go over and vote, Mr. Collins goes over and votes. That is relatively routine. Is that what is meant by that notion of routine?

That is a difficult one just as some of the other language is ambiguous. Some things are more routine than others.

Mr. RICHARDS. I think it does—from my point of view, I am not sure my colleagues agree—from my point of view it bears looking at again. If we can come up with better language, we can put it down on a piece of paper for you.

Mr. WIRTH. That would be very helpful. That has been one of the troublesome areas.

Any other comments on the question of what routine is? That is a major word that has emerged in the legislation as if there is magic to it.

Mr. RUNSER. You might find better wording. I wouldn't disagree with that.

We have this problem constantly in accounting. That is one reason why we have so much trouble today, because everybody in the accounting profession and in the legal area, in other areas, are trying to set standards and rules and specifics. It is a great problem to us. I think it is impossible because the rule will vary depending upon the given business circumstances.

Therefore, you can have guidelines or law to get rid of bribery, but I think there has to be a degree there where management can exercise their judgment in the given circumstances.

If they are wrong, they are going to get nailed and they should be nailed. That is why words like "routine, ordinary, reasonable," put the responsibility back on our backs where it belongs and leaves us room to operate.

Mr. WIRTH. I understand completely. You can't legislate good judgment. You can't legislate that kind of thing. What you can do is provide, as you were suggesting earlier, Mr. Runser, as clear a framework of what intent ought to be, and perhaps we can do a better job of defining routine, either in the legislative language or in the report, or find a different phraseology.

I want to be satisfied we have done the best job we can in defining that. I think Mr. Richards' suggestion of going back and taking a look at that would be very helpful. I think there may be some ambiguities there. Let's see if we can clear them up.

Any other routine comments here?

Mr. Collins, do you want to jump into this? I am going through what are some of the issues raised in all of this. I think we dealt with the accounting issue. We understand the concerns there. There are legitimate issues there.

I understand the arguments made on routine and why that maybe better than ministerial or clerical. Is "routine" the best we can do?

If not, let's try some more. Mr. Richards and company are going to help us on that.

Mr. COLLINS. Mr. Chairman, I am glad this is the last of the hearings so we can get on with the markup.

I know we are keenly interested in marking up so we can go to conference with the Senate. If we delay, we wouldn't have a bill. We all want to have a bill.

Let me ask you one thing. You all are senior executives in different fields. One feeling in Congress among some of the members is that businessmen sit around in dark rooms and plan how they can connive to get business. Have you ever—

Mr. WIRTH. Like politicians conniving to get votes?

Mr. COLLINS. This does happen in politics, but I was in business 25 years before I came here. I wanted to ask, have you ever had a senior officer of your company or a director of your company at any time in any way ever suggest or condone that you make any kind of a bribe or any type of an offer that is not completely within bounds?

Can you think of a single example of any officer or any director that would ever condone such activity?

Mr. RICHARDS. I would have to say to start out certainly not in our company. In fact, we have very stringent procedures that have been set up over the years to avoid this very thing domestically—and obviously even greater internationally—because in our Kellogg organization, we do something like 50 to 60 percent of our business overseas.

We have to be extremely careful to—particularly since the Corrupt Practices Act. I would have to say that in my experience, which goes back 37 years with the same company, I have never seen that.

Mr. COLLINS. I think you have a fine company. If you are going to stay in business basically you have to have a good reputation. Have you seen anything in your outfit?

Mr. RUNSER. No. As a matter of fact, I tried to describe how seriously our audit committee takes this. In attendance at a number of our audit committee meetings are the chief operating officer, the chief financial officer, the outside audit partner of a particular subsidiary. Let's say we are sitting down reviewing internal control comments. The audit committee sits there and they ask that chief operating officer, they say, have you had any kind of illegal foreign or domestic kind of payments, say, during the last quarter; and they report the findings of that, which there has been little or nothing, to the board of directors at their meeting.

So that question is asked specifically. That question they have to sign off on every quarter when they give us a representation letter.

Mr. COLLINS. Let me repeat that. You are thinking about it from an accounting and audit procedure. You are actually checking

quarterly or certainly annually on all of your foreign people to be sure they stay on the straight track?

Mr. RUNSER. That is so.

Mr. COLLINS. What have you found in Rohm and Haas?

Mr. SUBAK. I spent 20 years with a large law firm and only the last 6 years with a fairly good-sized chemical company. I must say by and large I find businessmen one heck of a lot more ethical, if you will, and much more inclined naturally to comply with law than the ones you have practicing law and more ethical than the ideas held by some people writing newspapers or who are in Congress.

My experience, Mr. Collins, has been—not just our company, but companies we deal with—are just pretty darned ethical outfits.

It is a pretty heartwarming thing to see.

Mr. COLLINS. You know basically what I can't understand is why we put this punitive burden on American business. I understand no foreign business carries this load on their shoulders.

Does any foreign business have to put up with this sort of thing? Do you know of any of them?

Mr. SUBAK. Quite the contrary. As most of you undoubtedly know, under the tax laws of Germany and England and other statutes, they indeed have amounts for which they do not have to account, which it is recognized is used for purposes of obtaining business.

So it is not just that they are not prohibited from some of the things which Americans are prohibited from doing, but indeed their tax and other laws fairly explicitly encourage it.

We are not urging that we go down that way, but, for example, one of the areas that has really gotten a lot of us concerned is the "having reason to know test."

Mr. Wirth was asking about ambiguities. There is nothing more ambiguous than a test of having reason to know with respect to the actions of someone else, a distributor, an agent, a company which you do not control.

I think it is fair to say that S. 708 sharpens that language very specifically.

Mr. COLLINS. That is right. The chairman mentioned whether or not you think it is a deterrent to us getting business abroad; whether it discourages our active participation and aggressive seeking of business abroad.

Do you really believe that it does act as a deterrent?

Mr. SUBAK. I think it is some deterrent. In the order of priorities, what is more important? To get a budget with a lower deficit than a \$100 billion, or amending the FCPA?

Well, obviously to get a budget through Congress.

I was sorry Mr. Wirth came back so soon. I was hoping he was going to fix it all up this morning.

Mr. WIRTH. Trying to be all things to all people is hard.

Mr. SUBAK. Yes, it is a real deterrent. I think anyone who lives with the act every day, as I do, recognizes it as such.

Mr. COLLINS. Let me ask one more thing, now. Is there any foreign country that in any way tries to come over to this country and tell their businessmen how to operate? I have never been familiar

with it. They are very aggressive in coming after business in this country in every way I can see.

In fact, I have just been most impressed at how much business we are losing in this country to foreign competition. I never have heard of this type of thing. Basically when we go abroad we impose requirements by which any top executive in this country can be responsible for some action abroad and that term that you used—and I am not a lawyer, but I have the same misgivings you do about how it can be misinterpreted.

Well, I want to thank all of you for being here. I thank the chairman. I do hope we will be able to get to mark up very soon.

Mr. WIRTH. Let me just for the record at this point point out we asked the Library of Congress to research the bribery laws of countries around the world.

The Library of Congress was not able to find a country where a bribe to an official in order to obtain a contract to sell a product was not illegal. It is not as if we are doing something unique here. It is part of the fabric of laws in every other country.

Mr. COLLINS. Mr. Chairman, may I ask, this is the first I knew about that. Have you heard of any country that has taken any type of action against any business that did business around the world as a result of that type of rather broad law? Have you ever heard if these laws mean anything?

Mr. WIRTH. Sure. That is what we are trying to do. That is how this came about to begin with. That is why I think somebody suggested Mr. Tanaka was in the slammer to start with. Isn't that correct?

Mr. RICHARDS. Another example is the recent Korean situation in Saudi Arabia where they threw them out of the country because of bribes paid to Saudi Arabian Government officials.

So it is quite surprising, but there it is.

Mr. SUBAK. I don't think it is one bit surprising that the rest of the world proscribes bribery in its own back yard. Indeed, in some places the penalties are a little more severe. You don't end up in the slammer; you may end up with an arm cut off or something like that.

The difference, Mr. Wirth, is the extra territorial effect of the law, and I believe that the United States is the only country which has an extra territorial application to the law and which proscribes bribery not of its own officials, but of the employees of other governments.

So that the research by the Library of Congress is obviously correct, but it doesn't really address the issue that we are talking about here.

Mr. COLLINS. Let's make this clear now. On that Korean situation, that was doing business in Korea, wasn't it?

Mr. RICHARDS. No; I believe it was doing business in Saudi Arabia—Korea. It was a Korean subcontractor.

Mr. WIRTH. We are not in the conversation, Mr. Collins, suggesting what we ought to do is eliminate the act. I don't think that is what anybody intends.

Let me, if I might, quote again from the—as I did, I believe, in the last hearing—from Mr. David Newsom, the former Ambassador to Libya and the Philippines, and former Assistant Secretary for

African Affairs, when he said to the subcommittee, "American businessmen often ask why us?" This is the discussion. "Why should Americans be singled out for restrictions when all around them their competitors appear to operate without such restrictions?"

To which Mr. Newsom answered his own question, which I think is why we are here today.

He said:

In my view it is a fact of international life that the corrupt association of a major American company with a foreign official carries political implications that relations with other foreign companies do not.

We cannot escape our political involvement as a major power. Our companies cannot escape the fact that their activities will never be totally detached from local sensitivities relating to U.S. intervention of any sort in the internal affairs of another country.

With which I think you all agree. That is why we are here. That is why you are being helpful in sorting out and defining this language which I would like to do with a few more specifics, if we might, before we close.

There are some other very specific items in the language that I was curious about.

Mr. Runser, maybe you can help us on this. There is in the Senate bill exclusions from applicability of the law for "facilitating or expediting payment," and "tokens of esteem."

Are those terms of art that are understood, facilitating or expediting payment, does that cause a problem? You could facilitate with the prime minister or with the guy running the dock. Do you see what I mean?

What is the difference between a payment to a prime minister which is a facilitating or expediting a payment and to a person who is unloading your goods at a dock?

I don't know what the answer is.

Mr. RUNSER. I have a summary of what is in S. 708, facilitating routine courtesies, tokens of esteem, hospitality, travel, lodging, expense, that versus ministerial or clerical in the law.

Now, to me, the rescission of indicators in S. 708 is a lot better than what is in the FCPA. That is all I can say.

It is more understandable to me in S. 708 than it is in the act.

Mr. WIRTH. If we are going to rewrite this, let's do it all the way through. If you read in page 8 of the Senate bill it says, "subsections (a) and (b), shall not apply to—any expediting or facilitating payment."

I am not sure if I were running an audit committee fresh to all this that I would say I am understanding what a facilitating or expediting payment is to whom and—

Mr. RUNSER. In the normal course of business. I think businessmen would know whether it was a bribe or whether it was something that all your competition was doing in that area to get something from the boat to the dock.

To me, that is pretty obvious. That versus a bribe.

Mr. WIRTH. The only question I am asking is whether "facilitating" is a term of art well understood, and "expediting payment"? You know, I consider a facilitating or expediting payment could allow you to do just about everything you could feel like doing.

Mr. SUBAK. Let me suggest, Mr. Chairman, that there were three different approaches tried before which would make life a little bit easier for the accountants. Those approaches were, one, to use the phrase "ordinary course of business," and that was shot down because it was felt that it was too broad an out.

Second, attempts were made to talk about nonmaterial amounts or immaterial amounts or another phrase that the accountants are used to, and these were again criticized as possibly allowing too large a number.

The third was the example I used before of an actual dollar amount and that got shot down on a quasireligious basis.

I don't think that there is a ready-made phrase from the accounting literature which is going to solve the specific problem that you are addressing, unless you are willing to take one of the traditional phrases, and I suggest that Congress has not been willing to do that.

Therefore, I think—

Mr. WIRTH. One of those being?

Mr. SUBAK. Either nonmaterial amount or ordinary course of business. Both of those the accountants would readily understand and be able to apply.

Mr. RUNSER. And it could vary from country to country.

Mr. SUBAK. That's correct. I would, therefore, suggest to you that you consider accepting the language that is in S. 708 and clarifying it in your committee or House report if you think that it ought to be clarified.

But the problem is what is routine governmental action?

Mr. WIRTH. Counsel tells me the problem with nonmaterial was what is material for one company is nonmaterial for another.

Is that the argument?

Mr. SUBAK. That's right. You allow the big guy to make a bigger payment than the little guy.

Mr. WIRTH. Is there in the accounting literature a definition of nonmaterial not relevant as to size of firm, but in which it is defined?

Mr. RUNSER. There is a definition generally accepted, that is, of material in the accounting literature and it goes to the threshold of the financial statements where you get to the problem of the big company versus the small company.

That definition of materiality in my opinion would not be useful for this test.

It would not be because materiality has a lot to do with the unusualness of a transaction or sensitivity of a transaction. So that when we are faced with an illegal payment, be it foreign or domestic, the materiality level, as far as the amount of dollars concerned, is very, very low because it is a very, very sensitive no-no.

The accounting profession has not gotten down the road of properly defining materiality. But we use it every day, but in a broad range.

That is why you would have a terrible problem using that.

Mr. WIRTH. So we cast that aside, right?

We are back to again to facilitating or expediting payment. As I read through S. 708, looking at it seems to me that it is ripe with ambiguities as well.

You have experience with the materiality standard. Is there some way that that can be defined so that it provides the kind of surety you are looking for?

Mr. RUNSER. In my opinion, I think it is difficult to get an absolute assurance or preciseness because the problem with routine or ordinary course of business changes with the given business circumstances which, in the foreign area, can change from country to country or port to port.

So how are you going to get words that are going to cover all that infinite matrix of business situations?

So, therefore, the judgment has to be left up to management and their responsibility to determine what is ordinary and routine and if they make a mistake, they are nailed with it.

Mr. WIRTH. Let me ask you a specific on that.

Mr. RUNSER. Put the responsibility where it belongs, on management.

Mr. WIRTH. Taking the next step to "ordinary." The Senate language says: "shall not apply to any ordinary expenditures, including travel and lodging expenses, associated with performance of a contract with a foreign government or agency therefor."

Is that a commonly understood definition of what ordinary expenditures are or does that leave room for uncertainty?

Mr. RUNSER. All I can say is I don't think there is any rule for that, but I understand those words. If a piece of paper or invoice came to me and it didn't fit that description, I think I would know whether to record it or not.

Mr. WIRTH. You wouldn't be here if you didn't understand that, that is why you are here and other people are not, but as a term of art, is it used in the accountant's world?

Does that word bring with it definitions any clearer than what we are talking about as facilitating or expediting payments or is that a judgment call?

Do you see what the problem is? "Ordinary, facilitating, expediting"—

Is there a better way of pinning down the definitions or is this as good as it is going to be?

Mr. RUNSER. I think all the words you have used are broad enough to cover. The principle is to allow judgment within the given business circumstances. If you get too precise with it, everybody is constrained and they get in doubt of what to do or not to do.

This broadens it so that we who have the responsibility can exercise our judgment in the circumstances. If the public agrees with Mr. Subak and his comment, I happen to agree, I think most corporations in this country act with a heck of a lot of integrity.

Mr. WIRTH. I do, too.

Mr. RUNSER. I can't say there are no bad apples in the barrel, but why should 99 and 44/100ths of them be punished for the few bad ones?

Mr. WIRTH. That is what happens. We all live in that world and that is what a world of law generally is all about, isn't it because you have to define conflicts and you have to define what you do with the rotten apples?

That is how we got into this to begin with.

Can you interpret ordinary expenditures if you are dealing with X country as meaning bribes? If that is an ordinary expense in that country, how do you make the distinction between a grease payment and bribe as an ordinary expenditure?

Mr. RUNSER. Bribes are outlawed by the act. That will stay. If it is a bribe, you better not pay it.

Mr. WIRTH. But the problem is under the Senate bill, "ordinary expenditures" are an exception to the bribery provisions.

You can't pay bribes but you can if they are "ordinary expenditures".

It is for us to play Devil's advocate to make sure this is clear, Mr. Runser. Bribes are precluded, right?

Mr. RUNSER. Right.

Mr. WIRTH. But you can pay a bribe if it is under ordinary expenditures?

Mr. RUNSER. I wouldn't agree with that. A bribe is not allowed, period.

Mr. WIRTH. But that is not what the language of the bill says.

Mr. RUNSER. I don't interpret a bribe as a normal, routine expenditure.

Mr. WIRTH. I don't think we can have a circular argument that says, we will preclude bribes, but if bribes fall under ordinary expenditures, then they are an exception to the prohibition against bribery.

There is this circular situation and a good attorney could come in and capitalize on these ambiguities. That is what we want to get rid of.

Mr. RUNSER. That linkage could be made so it is clear.

Mr. WIRTH. I don't know how to do this.

Mr. Richards was going to help us. Do you see the problem? There is a circular nature to that exception which we ought to pin down if we rewrite this, again, let's go and do it as well as we can.

I know you have been struggling with this, Mr. Subak.

Mr. SUBAK. Yes, but it doesn't just say any ordinary expenditures, the clause is any ordinary expenditures, including travel and lodging expenses associated with the performance of the contract.

So that I think that a fair interpretation of that provision by any court would be talking about a different type of expenses, room, board, meals, expenses of that sort.

The payments as such are quite specifically addressed in subsections (1), (2), and (3), so when the Senate wanted to talk about payments, they knew how to do it. Sections (4) and (5), really, talk about out-of-pocket expenditures, travel, lodging, that type of expense.

I am not suggesting that the wording is perfect, but I am saying that (4) and (5) are really not a backhanded, nor a circular way of permitting that which is forbidden by the basic statute.

Mr. WIRTH. The Senate language has come under criticism for exactly that, that is, what I am going after, that it is a loophole or backhanded way of doing it when you get to (4) and (5).

(4) says "any expenditures . . . associated with selling or purchasing of goods and services," (5), is "any ordinary expenditures associated with the performance of a contract."

Mr. SUBAK. If I wanted to write a loophole, I would do a better job.

Mr. WIRTH. That is not the point, Mr. Subak, I am not suggesting somebody is trying to write a loophole, all we are trying to do is go right to the ambiguities, and that is how we got into this. Again, let's not replace one ambiguity with another if we can help it.

Let's recognize where they are and take a look and see if we can clarify the ambiguities, as Mr. Richards suggested in our earlier discussion. If the questions of "any ordinary expenditures" and expediting or facilitating payments are as good as we can do, fine, if not, there is other language perhaps that we can use.

I am not trying to be contentious on this, but I am suggesting we are looking at ambiguities and trying to eliminate it. That is the purpose.

That is what you want. We hear it over and over and over again and we want to do the best we can.

Mr. RICHARDS. It seems clear to me that one of the purposes of a hearing like this is to get all of the problems that you, as chairman, and that the committee have, out on the table and we who have been working on this issue and trying to—

Mr. WIRTH. You know a lot more than we do, we need your help.

Mr. RICHARDS. We will do things we think will improve business possibilities in the future and increase our exports and increase jobs.

I think that a lot of active work has been done on getting the language together here by many people who are certainly more expert than I am and I think we ought to look at these and sit down with your committee people and work it out and see if we can come up with better language or stay with the language of S. 708.

Mr. WIRTH. Maybe we end up with one thing, maybe that is all there is there, but I don't see—we are not tied to S. 708. Everybody wants to clarify this. That is the sense of the committee.

Let me go to one other issue. One of the biggies which I saved till last is the "reason-to-know" language. That is probably the language that we hear the most about as causing a feeling of ambiguity. We hear that attorneys have counseled companies against going into various ventures because of the difficulty of the "reason-to-know" language.

As you know, the language was added to the 1977 act to reach those situations in which American companies pay bribes through third parties.

That was the reason that "reason-to-know" language was there.

The Justice Department told us last fall that of the cases that were under investigation under the act, it was the third-party situations that dominated the number of cases, about two-thirds of the cases they were looking at involved payments through third parties.

So there was a problem everybody recognized; that is why "reason-to-know" was included.

The case has been made that the "reason-to-know" language does not exist elsewhere and that it is ambiguous. In fact, we did a search of the U.S. Code and the "reason-to-know" language is found in more than 20 other statutes.

So it is not a freestanding set of legislative provisions but it is well understood and is found in a variety of other statutes and was borrowed from other statutes for that reason.

In S. 708, the Senate replaced the "reason-to-know" language with "course-of-conduct."

Let me read it.

It shall be unlawful for any domestic concern or any officer, director or employee or shareholder thereof, acting in behalf of such domestic concern, to make use of the mails or any means or instrumentality of interstate commerce corruptly to direct or authorize expressly or by a course of conduct a third party in furtherance of a payment gift, offer or promise of anything of value to a foreign official.

We have researched "course of conduct," and there is no definition of what we mean by "course of conduct."

Again, the question I am asking is, are we replacing one set of language, "reason-to-know," which has a long legislative history, and a great deal of court interpretations as to what that means, with something that provides a different set of ambiguities.

The Senate goes on to define the "course of conduct" as being a "course of conduct." If we read the Senate report language, it says "the committee intends the term 'course of conduct,' used with the term 'authorized' in section 104(b), to refer to those situations where a company, through its words or course of conduct, has intended the corrupt payment be made."

In other words, we define "course of conduct" by "course of conduct."

Now, the question is, one, the "reason-to-know" language—as ambiguous and difficult as it's been suggested to be—should that be more clearly defined in the statute or in the report? That is one approach to clear up what we have heard again and again, are ambiguities.

Can that be defined?

Or, if it cannot be defined and should be replaced, should it be replaced with something like course of conduct which, from the research that we have been able to do on it, has no history on that front and is, in the Senate report, a self-defining term?

You see that? Should we look at "reason-to-know" and define it so the ambiguities that people talk about are clarified? Or should it be replaced with other language and, if so, does "course of conduct" do the job adequately?

Can you respond to that, Mr. Subak?

Mr. SUBAK. Yes. Having "reason-to-know" has a history of being ambiguous. We are now starting afresh with a new concept. We know that there are problems with it.

Let me give you a specific example. You are appointing a distributor in Country X and you read a newspaper account which says that distributors in Country X typically make improper payments.

You go out of your way to find a distributor who is fully ethical, does that newspaper story give you reason to know that improper payments are going to be made?

I can assure you from personal experience that the reason-to-know test applied in this context is very, very troublesome and the one we find the most difficult to work with.

Your question, then, is—let's agree it is broke, but have we fixed it?

It is better than having reason-to-know. How good it is, I guess we may have to wait a while to see what the reports say about it, to see what the courts might say about it.

It didn't get there by accident. The language some people would have preferred would simply have limited the prescription to those payments which are directed or authorized.

The concern was, well, that allows the head-in-the-sand approach, and, therefore, the expressly or "by course of conduct" got in there.

Is it the best phrase? I don't know. I can't think of a better one. It is a lot better than the test of having reason to know.

Mr. WIRTH. Mr. Runser, would you care to comment?

Mr. RUNSER. No.

Mr. WIRTH. Well, should course of conduct become the operative and directive phrase in the law? The question we would have, as I read the research done on "reason-to-know" is, is there that much ambiguity in "reason-to-know"?

From the summary analysis we had done of the "reason-to-know" language, it is in over 20 Federal criminal and civil statutes.

The data prepared for us on this noted that the phrase in other statutes has been interpreted by some courts in criminal cases as meaning actually knowing.

Mr. SUBAK. If you want to put in "actually knowing," fine, but I don't think that's been suggested so far.

Mr. WIRTH. Our research also noted that the reason-to-know language, as modified by the word "corruptly," means there is an evil motive requirement under the law.

Reason-to-know modified by the word "corruptly," brings with it a lot of court precedence to interpret the law, rather than trying to break new ground with new language that people don't understand.

Do you have any problem with that?

Mr. SUBAK. I would—

Mr. WIRTH. You would like to get rid of the "reason-to-know language," right?

Mr. SUBAK. The "reason-to-know" test may let you win a court case, but it is not one that I am willing to live with on a practical day-to-day basis.

Mr. WIRTH. What can we do to define it? We have on the one hand the desire to win a court case and be on firm ground in the courts, which is what you, as a prudent lawyer, would want to advise your client.

On the other hand, you want to be able to give them the best advice on whether or not they should go into a particular foreign venture, and you are saying that the current "reason-to-know" language inhibits them from going into that venture, and you, as a prudent lawyer, would advise them not to do so.

Is there a way in which we can define the reason-to-know language, because it has a long history, in a way that you would feel comfortable about it?

Mr. SUBAK. I am beginning to feel like one of my kids, Mr. Chairman, when they say, "Gee, I like it, dad," and I keep saying, "No, son, you don't like it." We are willing to sign on with the Senate bill.

Mr. WIRTH. I understand that.

Mr. SUBAK. We like it. We think that it does cure the ambiguities and you keep telling us, "Gee whiz, you guys, you shouldn't like it because you are trading one set of ambiguities for another."

I say, "Gee whiz, dad, I really like it."

Mr. WIRTH. That is our job, isn't it? The reason we got into it is because of the uncertainties that people say exist in the current law.

If I, the chairman, a nonlawyer looking at the language, recognize a variety of uncertainties in S. 708, and if the current law is said to be ambiguous, but has a set of court precedents, where do you get when you create new language.

I don't want to be back here 2 years from now with people saying we have this ambiguous language, we got the legislation out, we feel macho good, but we really haven't done anything.

Wouldn't be here if there weren't a lot of people raising the question of ambiguity. That is how we got here and I would suggest there are still ambiguities. The job we have, Mr. Subak, is to be sure we are clarifying it and not ramming through something for the purpose of putting it through.

That may not be the case, but that is the job I have. I am doing this exercise as a prudent Congressman, just as you advise a client to go into a business as a prudent lawyer, right?

So let's respect each other's professionalism and not compare that to an adolescent's desire of "I like it," or "I don't like it."

I don't think that gets us to the point where we want to be.

If, Mr. Richards, there is a possibility of looking at the "reason-to-know" language, I would appreciate your doing that.

I do not understand how a "course of conduct" is defined. There is not a place in the law where it says what it means. It is defined in the Senate report as "course of conduct." That doesn't seem to me that that is a very good definition.

Again, the purpose is to sort out ambiguities.

If your group could look at that, it seems that is a bigger ambiguity, than the ones we have talked about.

Mr. RICHARDS. I do know there is a tremendous amount of effort in our experience sufficient to look at this particular issue.

I can't say I am in any way an expert on it, but I do think it is one that we can have another go at, as the British say. We can see if there is a way to improve it.

It occurs to me that this is something that should be ironed out in the conference. These three particular issues. It would appear that most others you seem to be pretty much in agreement with.

Before that, I will take then into account, as a charge, to go ahead on these three particular points and see if there is some way we can look at the specific language in a more substantive way.

Mr. WIRTH. I am not an expert, you know.

Mr. RICHARDS. And I am not a lawyer.

Mr. WIRTH. I am a lay legislator reading the language. All the people are saying it is ambiguous, so let's not do it that way, let's try to do it right.

I learned a couple of things from my chairman, Mr. Dingell, over the years of being a student of his. One of those is that you keep

the feet to the fire as much as possible until you get it as well as you possibly can.

Second, you do the best job you can in the subcommittee and you don't wait for conference, and you do the best job you can in full committee and you don't wait for conference, and you do the best job on the floor and don't wait for the conference, the conference being a last resort.

That is an appropriate charge and the way Mr. Dingell runs this committee. You do them the best way you can and you get satisfied you have done the best job you can and maybe somebody has a better idea at some later point.

Nobody is sitting here saying we don't think there are ambiguities in the law, right? We have been beaten up by some saying that we are not concerned. But that is not the case.

We just want to get the rhetoric out of the way and get down to the details of this and not try to bury the head in the sand in any fashion.

That would be very, very helpful, sir, if we could get your group to work on that and that would be very constructive and productive.

I might add we have asked the administration to do that and they have come back and said, we can't do anything more, having promised us they would look at it, we have not gotten anything really constructive.

So let's try somewhere else and see.

Mr. RICHARDS. I believe the STR has written with some comments on the changes, but I am not familiar with all the details of that.

We will look at that again.

Mr. WIRTH. We have been trying to pull those teeth, too.

Any final words for the good of the order before we adjourn this?

I think we are all thoroughly anesthetized by the Foreign Corrupt Practices Act. Maybe that is enough anesthesiology for the morning.

Thank you for being with us.

The subcommittee will be adjourned.

Thank you.

[The following statements were received for the record:]

STATEMENT OF DAVID D. NEWSOME, DIRECTOR, ADMINISTRATION AND PROGRAMS,
INSTITUTE FOR THE STUDY OF DIPLOMACY, GEORGETOWN UNIVERSITY

Mr. Chairman and members of the sub-committee:

I am pleased to be given this opportunity to assist your sub-committee in its consideration of the important and difficult questions which relate to the Foreign Corrupt Practices Act.

As an Ambassador of the United States in three countries, Libya, Indonesia, and the Philippines where U.S. trade is significant, and as a former Assistant Secretary for African Affairs, I am aware of the significance of the issue. No one with any preception can serve abroad and be unaware of the fact that favors of one kind or another to foreign officials are a factor in decisions on major government contracts and on the granting of licenses and franchises to do business in many countries.

At the same time, evidence of specific instances in specific countries is difficult to obtain. The sensitivity both of officials and business men leads them to seek to mask the practice and the results. It is impossible not to be aware, however, of the often close relationships and favors of company agents to government officials or of the life style of middle level foreign officials beyond any limit their known salary would support.

Appearances and gossip also lead the American abroad to conclude that the practice is common among the representatives of some of the closest national competitors of the United States. These countries, which have a greater dependence on exports than we, not only give strong diplomatic backing to their exporting companies but clearly make little effort to curb favors to foreign officials on behalf of their exports.

As far as the practices of American companies are concerned, the American Ambassador may well be the last to know. The Ambassador has no authority to inquire into such activities. My own experience in talking with business representatives suggest that they each will tell you he is as pure as driven snow;

it is the other Americans and the foreign competitor who are involved.

Are such practices necessary if the American business man is to compete successfully abroad?

I am not familiar in detail with the legislation currently before the sub-committee. I have read the previous testimony of Ambassador Brock, Ernest Johnson and Mark Feldman before the sub-committee of the Senate dealing with this matter. From that I understand that one of the objectives is to clarify the law relating to payments made to facilitate or expedite the performance of official duties and relating to gifts and tokens of regard. I would think that, where there has been ambiguity in these areas, it is necessary to clarify it. We cannot ignore long-standing practices in countries where the civil servant pay is barely at the living level.

The main issue relates to substantial payments in pursuit of major government contracts or licenses.

My own observations would suggest that an American company with unique technology, capital, a good local training program, and a willingness to share equity with local interests can, so to speak, enter by the front door.

If a company is in strong competition with a foreign firm with like - or possibly even superior-technology and favorable credit terms, the entry may be more difficult. The same can be said where a foreign company is competing with a local company.

In either event, as an Ambassador I have urged those American business men who have sought my counsel abroad to begin by an approach to the appropriate government officials without any assumption that extra favors are necessary. In each of the countries in which I have served and in many I have observed in Africa there are senior officials who want to reduce the incidence of corruption. They may, provided they are themselves enthusiastic about a proposal, have

sufficient influence to persuade a head of government to accept a proposal without favors.

I have seen too many business men who assumed that they had to seek out a relative of a high official or have been sought out by go-betweens before ever approaching those ostensibly responsible for decisions. The foreign business men become involved and obligated before the legal approach has ever been tried. Many have been stung in the process and it is up to the Embassy frequently to try to extricate them. The practice of corruption cannot be ended if business men are not prepared at least to give the honest route a try.

I cannot say how many American companies may have lost out in competition abroad because of this nation's scruples against illicit payments. I can say that, in my view, it is clearly in the foreign policy interests of the United States to discourage such practices.

In my career, I have seen at close hand circumstances leading up to two revolutions, in Iraq and in Libya. In both, significant U.S. interests suffered. In both, the degree of corruption in the regime was a factor in the opposition and in the loss of public confidence which made a successful revolution possible. In other countries today where we have significant interests, similar circumstances prevail.

It is not necessarily clear evidence of corruption that leads to the weakening of friendly regimes. It can be a public perception of corruption, arising from the significant and ostentatious accumulation of wealth by senior government officials, the knowledge of manipulated bids in important projects and the conspicuous association of government officials with the agents of successful foreign bidders.

American business men often ask, "Why us?" Why should the American be singled out for restrictions when all around them their competitors appear to

operate without such restrictions. In my view it is a fact of international life that the corrupt association of a major American company with a foreign official carries political implications that relations with other foreign companies do not. We cannot escape our political involvement as a major power. Our companies cannot escape the fact that their activities will never be totally detached from local sensitivities relating to U.S. intervention of any sort in the internal affairs of another country.

The testimony of Department of State witnesses before the Senate sub-committee referred to the efforts of this government to bring about an international agreement on corrupt practices. This is highly desirable. As our efforts to get an international agreement on levels of export credits have demonstrated, however, the achievement of such an agreement may be very difficult. Other countries with a greater stake, in their view, in exports, may not be prepared to apply the same limits to their business men.

We should keep trying, but we should not be under any illusions about early results. And, given our own peculiar standing in the world, we may clarify but we should not weaken our own restrictions or resolve while waiting for international agreement.

David D. Newsom

[Whereupon, at 12:41 p.m., the hearing was adjourned.]

